(4)

No. 90-727

Supreme Court, U.S.
FILED
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In The

Supreme Court of the United States

October Term, 1990

ROBERT G. HOLMES, JR.

Petitioner,

vs.

SECURITIES INVESTOR PROTECTION CORPORATION, et al.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

JOINT APPENDIX
VOLUME I

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Petition For Certiorari Filed November 1, 1990
Certiorari Granted April 22, 1991

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CHRONOLOGICAL LIST OF RELEVANT DOCKET ENTRIES

DATE	NR	NO.	PROCEEDINGS
09/27/84	am	248.	First Amended Complaint; demand for Jury Trial. Issued Summons. Pltfs.
11/26/84	as	275.	Notice of motion by Defendant Robert Holmes, Jr. to dismiss the complaint; memo of Points and Authorities. 3/4/85 at 10:00 a.m. Deft. Holmes, Jr.
11/26/84	as	278.	Defts. consolidated memo in support of motion to dismiss based on lack of SIPC standing, 3/4/85, 10:00 a.m. Deft. Creditbank.
11/26/84	as	279.	Notice of consolidated motion of Defts. to dismiss first Amended Complaint based on lack of SIPC standing, 3/4/85 at 10:00 a.m. Deft. Creditbank.
11/26/84	sb	284.	Notice of consolidated motion of Defts. to dismiss first Amended Complaint based on lack of Trustees standing, 3/4/85, 10:00 a.m. Deft.
01/10/85	as	313.	Pltfs memo of Points and Authorities #2 in opposition to motion to dismiss Trustee claims for lack of standing and Holmes motion to strike Pltfs prayer for punitive damages, 3/4/85, 10:00 a.m. Pltf.

01/10/85	as	315. Pltfs memo of Points and Authorities #3 in opposition to defts consolidated motion to dismiss claims of Securities Investor Protection Corp for lack of standing, 3/4/85, 10:00 a.m. Pltf.
01/17/85	as	320. Exhibit A to pltfs memo of Points and Authorities #2, in opposition to Dfts consolidated motion to dismiss trustee claims for lack of standing, Holmes motion to strike pltf prayer for punitive damages, 3/4/85, 10 am pltf
02/11/85	as	326. Defts Consolidated reply memo in support of motion to dismiss based on lack of SIPC standing 3/4/85, 10:00 a.m. Deft. Creditbank.
02/11/85	as	328. Reply by deft Robert G. Holmes Jr. to pltfs memorandum of Points and Authorities #2 in opposition of deft motion to dismiss and Holmes motion to strike pltfs prayer for damage, 3/4/85, 10 am Deft
02/11/85	as	330. Defts. consolidated reply memo in support of motion to dismiss Trustee Claims, 3/4/85, 10:00 a.m. Deft.

03/04/85	sb	338. Court order motion to dismiss lack of Trustees standing and lack of SIPC standing denied and court grants SIPC 10B claim and denies SIPC motion: to dismiss denied without prejudice mont to dismiss RICO Deft. lack of personal jurisdiction denied and court order motion denied motion withdraw reference to Bankruptcy granted as to adversary proceeding status conference 9/9/85 at 3:00 p.m. mo
03/14/85	kw	342. ORD (1) references to Bankruptcy Court of adversary proceeding entitled Securities Investor Corp. vs Garrity (in Garrity, BK #SA85-00083-PE, Adv. #SA85-0138-PE ("Garrity Action") is withdrawn and all proceedings in that action be taken before this court.; (2) Garrity Action is consolidated with SIPC Action for all purposes; (3) case #CV-83-5674-AWT (Tx) Cain vs Vigman is consolidated with SIPC Action for purposes of discovery; (4) pltfs claims against Frankie Mae Garrity and Rodger W. Garrity in SIPC Action only are severed from all other claims in the consolidated actions for all purposes; (5) this Order be filed in SIPC Action, Garrity Action, and Cain Action; (6) pending further Order of Court, all pleadings and papers shall be filed in #CV-83-4742-AWT (Tx); and as further stated.

03/15/85	as	341. ORDER certifying issues for Interlocutory Appeal and Order granting motion to dismiss for lack of standing SIPC's Exchange claim and DENYING motion to dismiss for lack of standing the common law fraud claims, all. (Entered 3/19/85 mailed copies/notices).
03/22/85	as	345. Notice of Order certifying issues for interlocutory appeal and alternatively for entry of Judgment. Pltf.
04/03/85	as	349. ANSWER OF DEFT. ROBERT G. HOLMES, JR. TO First Amended Complaint Deft. Holmes Jr.
04/11/85	avm	377. Pltf's NOTICE OF APPEAL to 9th Circuit Court of Appeals from Order dated 3/19/85. $70 filing and docket fee paid. Mailed copies to all parties.
07/29/85	vu	LODGED copy of judgment from 9th Circuit reversing and remanding US District Court.
08/05/85	vu	451. ORDER that mandate of 9th Circuit Court of Appeals reversing and remanding is filed and spread upon minutes of this US District Court; in accordance with mandate, dismissal against Eugene C. Ferri, Jr. and Mobile International Corp. is vacated; Pltfs granted 30 days in which to further amend their pleadings as against said Defts. (Entered 8/9/85); Mailed copies to parties.

02/26/87	esl	734. Court ORDERS from 9th Circuit Court of Appeals reversing and remanding appeal filed and spread. MO. (N/R) (Entered 2/27/87).
02/26/87	la	LODGED proposed order from 9th Circuit Court of Appeals judgment reversed and remanded.
08/12/88	bc	1273. Exhibits to motion of Deft. for Summary Judgment on issue of causation; declaration of Richard Walker. deft. Robert Holmes Jr.
08/15/88	bc	1274. Exhibits to motion of Deft. Holmes for Summary Judgment on issues of claim asserted under the RICO Act. Deft. Holmes.
08/15/88	bc	1275. Notice of motion and motion for Summary Judgment; returnable 10/17/88 at 10:00 a.m. Deft. Holmes. LODGED prop statement of uncontroverted Facts and Conclusions of law. LODGED prop Summary Judgment.
08/15/88	bc	1276. Memo of Points and Authorities in support of motion for Summary Judgment. Deft. Holmes.

08/15/88	bc	1277. Notice of motion and motion for Summary Judgment with respect to claims asserted under the racketeer influenced and corrupt organizations act. Returnable 10/17/88 at 10:00 a.m. Deft. Holmes. LODGED prop statement of uncontroverted Facts and Conclusions of law. LODGED prop Summary Judgment
08/15/88	bc	1278. Memo of Points and Authorities in support of motion for Summary Judgment. Deft. Holmes.
08/15/88	bc	1279. Exhibits to motion for Summary Judgment. Deft. Holmes.
08/15/88	r/s	1281. Notice of Motion and motion for Summary Judgment issue of causation, returnable 10/17/88 at 10:00 a.m. Deft. Robert Holmes, Jr.
08/18/88	r/s	1282. P/S of exhibits to motion by personal service to Joel A. Bonner, Karen Marse, and Marc Seltzer on 8/15/88. Deft. Robert Holmes, Jr.
08/18/88	r/s	1283. P/S statement of uncontroverted facts by personal service to Joel A. Bonner, Karen Maarse, and Marc Seltzer on 8/15/88. Deft. Robert Holmes, Jr.

08/18/88	r/s	1284. P/S uncontroverted facts and conclusions of law by personal service to Joel A. Bonner, Karen Maarse, & Marc Seltzer on 8/15/88. Deft. Robert Holmes.
09/16/88	r/s	1290. Amended Notice of Motion and motion for Summary Judgment that SIPC lacks standing to assert claims under 1934 Securities Exchange Act, Section 10(b) and Rule 10b-5. Deft. Robert G. Holmes, Jr.
09/21/88	r/s	1308. Opposition to Deft. Holmes motion for Summary Judgment for lack of causation. Pltf Securities Investor Protection Corp.
09/21/88	r/s	1309. Declaration of John B. Torkelson support of pltf opposition to Deft. Holmes motion for Summary Judgment. Pltf Securities Investor Protection Corp.
09/21/88	r/s	1310. Declaration of James C. Foley support of opposition of Pltf, Pltf Securities Investor Protection Corp.
09/21/88	r/s	1311. Pltf statement of genuine issues of material facts, pltf Securities Investor Protection Corp.
09/21/88	r/s	1315. Statement of genuine issues of material facts, Pltf Securities Investor Protection Corp.
09/21/88	r/s	1317. Statement of background and facts, Pltf Securities Investor Protection Corp.
09/21/88	r/s	1318. Statement of genuine issues of material facts, Pltf SIPC.

09/21/88 r/s 1319. Memo of Points and Authorities opposition to Deft. Holmes motion for Summary Judgment, Pltf. SIPC.

09/21/88 r/s 1321. Memo of law in Joinder with pltf opposition to Deft. Holmes memo of Points and Authorities support motion Summary Judgment with respect to claims under racketeer, pltf Randall Cain.

09/22/88 r/s 1293. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. I, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1294. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. II, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1295. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. III, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1296. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. IV, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1297. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. V, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1298. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. VI, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1299. Appendix of evidence in support of statement of background and facts in opposition to Holmes motions for Summary Judgment, Vol. VII, Pltf Securities Investor Protection Corp.

09/22/88 r/s 1302. Memo of Points and Authorities in opposition to Deft. Holmes motion for Summary Judgment with respect to claims under Racketeer Influenced & Corrupt Organization Act.

09/26/88 r/s 1304. P/S of Plaintiffs appendix of evidence support of statement of background and facts in opposition to Holmes motion for Summary Judgment, Vols 1-7. by mail on 9/22/88 to (attached list). Pltf Securities Investor Protection Corp.

09/26/88 r/s 1305. P/S of Pltf appendix of evidence support of statement of background and facts in opposition to Holmes motion for Summary Judgment, Vols 1-7, by personal service 9/22/88 to Robert G. Holmes, Jr., for Deft. Law Offices of Buchalter, Nemer, Fields & Younger.

09/26/88 r/s 1306. P/S of Pltf appendix of evidence support of statement of background and facts in opposition to Holmes motion for Summary Judgment, Vols 1-7, by personal service to Frandzel & Share for Defts. Dash Industries Inc., Jay Dash and Phillip Dash, Pltf Securities Investor Protection Corp.

09/26/88 r/s 1307. P/S of Pltf appendix of evidence support of statement of background and facts opposition to Holmes motion for Summary Judgment, Vols 1-7, by mail on Sept, 1988 to Lester L. Levy, Esq. Pltf Securities Investor Protection Corp.

09/29/88 r/s 1320. Memo regarding Deft. Holmes motion for Summary Judgment that SIPC lacks standing to assert claims. Pltf Randall A. Cain.

09/30/88 r/s 1322. Supplemental appendix of evidence support statement of background, pltf Securities Investor Protection Corp.

10/13/88 r/s 1326. Reply to Pltf opposition to motion for Summary Judgment, Deft. Robert Holmes.

10/13/88 r/s 1327. Reply memo with respect to claims under racketeer influenced, Deft. R. Holmes, Jr.

10/13/88 r/s 1328. Reply to Plaintiffs opposition to motion for Summary Judgment that SIPC lacks standing, Deft. Holmes, Jr.

10/24/88 r/s 1337. Surreply to Holmes reply to pltf opposition to Summary Judgment motion on causation, Pltf Securities.

10/24/88 r/s 1338. MO: Summary Judgment motions taken under submission. Court Order Dash dfts motion to continue Pretrial Conference GRANTED in part. Pretrial Conference date is continued to 01/-9/89, @ 03:00 PM. Court Order case set for Status Conference on 12-05-88, @ 01:30 PM. Court directs attorney for Dash to prepare form of Order.

10/26/88 r/s 1340. Statement of Uncontroverted facts in support of Motion for Summary Judgment that SIPC lacks standing to assert claims – Deft. Robert G. Holmes, Jr.

10/26/88 r/s 1341. Judgment and Order for Partial Summary Judgment – IT IS ORDERED that SIPC lacks standing to assert claims under Securities Exchange Act of 1934 against Robert G. Holmes, Jr. SIPC's 2nd & 16th claims for relief against Holmes are DISMISSED in entirety with prejudice. (Entered 10/28/88).

10/31/88 esl 1342. STATEMENT OF UNCONTROVERTED FACTS & CONCLUSIONS OF LAW & ORDER. (Entered 11/3/88).

10/31/88 esl 1343. ORDER granting Summary Judgment (RICO claims) it is hereby ORDERED that deft. G. Holmes, Jr.'s motion for Summary Judgment with respect to claims asserted granted and such claims are hereby DISMISSED. (Entered 11/3/88).

10/31/88 esl 1344. Summary Judgment (HOLMES) ORDER that this motion for Summary Judgment is granted and judgment shall be entered forthwith as requested in the motion in favor of deft. Robert G. Holmes, Jr. and against Pltfs. (Entered 11/3/88) Mailed copies to all parties.

11/28/88 r/s 1352. Notice of Motion and motion for Order granting leave to file interlocutory appeal, and stay all proceeds pending appellate review, returnable 12/19/88 at 9:30 a.m. Pltf Securities Investors.

11/28/88 r/s 1353. memorandum of Points and Authorities support of Motion for leave to file interlocutory, Pltf Sec. Invest Protect

11/28/88 r/s 1354. Notice of Joinder and joinder in motion of pltf for leave to file interloc, Pltfs

12/05/88 r/s 1355. Memo re motion for leave to file interlocutory appeal, or entry of final judgment, Deft. Holmes.

12/06/88 r/s 1356. Statement re SIPC's Motion for leave to file interlocutory appeal, etc., Defts. Diamond, & McNeil.

12/09/88 r/s 1364. Reply brief in support of motion for Order Granting leave to file interlocutory appeal, or enter Final Judgment and for stay of all proceedings pending appellate review, Pltf

12/16/88 r/s 1365. Surreply brief of Robert G. Holmes, Jr. re Pltf motion for leave to file interlocutory appeal, or entry of final judgment, Deft. Holmes.

12/19/88 r/s 1366. Response to surreply of Holmes re pltfs motion for leave to file interlocutory appeal, Pltf

12/19/88 r/s 1368. MO: Order motion to file interlocutory appeal GRANTED and motion for general stay also GRANTED with three exceptions. Stay applies to Class Action as well, RP

12/22/88	am	1369.	ORDER that each of the order's granting Summary Judgment and the summary Judgment in favor of Deft. Robert G. Holmes, Jr., against pltfs disposing all claims by pltfs against defendant Holmes hereby is amended to include an express determination that there is no good reason for delay and an express direction for the entry of judgment. Further that all further proceedings in this action and in the action consolidated herewith are stayed pending appeal or until otherwise ordered by the court except Any activity including motions, stipulations and orders to negotiate and complete any settlement; Mont. for entry of default judgment against Deft. Lugo and any discovery activity with the prior approval for the court for good cause shown for an exception from the stay. (Entered 12/29/88) copy to parties.
01/06/89			Notice of Appeal of Plaintiff SIPC.
01/10/89		1370.	Notice of Appeal of Plaintiff SIPC.
01/20/89		1373.	Notice of Appeal; U.S.D.C. Docket (Filed in U.S.D.C.)
04/13/90	r/s	1414.	Notice of joinder in motion for Order determining class settlement and barring claims against settling deft Robert G. Holmes, Jr., deft

04/30/90	r/s	1416.	MO: crt approves partial settlement and bars claims against settling defts stated above, including Holmes. Court grants with out argument pltfs application for reimbursement of costs and expenses., court takes under submission Trustees request to audit claims and the plft application for award attorney fees, LAH
05/02/90	r/s	1417.	FINAL JUDGMENT AND ORDER DISMISS: court approves settlement as set forth in Stipulation; Court directs entry of this Final Judgment and Order of dismissal as a final judgment.
		1418.	ORDER determining class settlement to be in good faith and barring claims against settling defts Magnetic Technologies Corp, Gordon McNeil, Isadore Diamond, Seymour Vigman, and Aero Systems, Inc., Defts
10/01/90	jh		LODGED cc Order from 9th Circuit Court of Appeals reversing and remanding.
10/05/90	jh	1425.	MO: Upon the filing of the mandate of the Court of Appeals, reversing the grant of Summary Judgment against pltfs on THE RICO claim, ORDER Status Conference is set for 10/29/90 at 3 p.m.; any party may file a separate Status Conference report Not Later Than 10/22/90, C/R none.

10/05/90	jh	1426. MO: Court ORDER that mandate of 9th Circuit Court of Appeals the record reflects that costs of the prevailing party were taxed by the 9th Circuit Court of Appeals in the amount of $1,819.02 on 9-25-90 (89-55094) and $3,730.43 on 9-25-90 (89-55094 and 89-55128) is hereby filed and spread upon the minutes of this District Court (ENT 10-10-90)
10/22/90	lp	1430. Stipulation and ORDER staying proceedings pending application for review.

COURT OF APPEALS

02/03/89	DOCKETED CAUSE AND ENTERED APPEARANCES OF COUNSEL. Sent appellant(s) civil appeals docketing statement, setting schedule as follows: Fee payment is due 2/17/89; CADS due 2/17/89 for Stephen C. Taylor; appellant's designation of Reporters Transcript is due 1/17/89 for Securities Investor; appellee's designation of Reporters Transcript is due 1/26/89 for Robert G. Holmes; appellant shall order transcript by 2/6/89 for Securities Investor; court reporter shall file transcript in District Court by 3/8/89 for Patt Lawler; certificate of record shall be filed by 3/15/89; appellant's opening brief is due 4/24/89 for Securities Investor; appellees' brief is due 5/24/89 for Robert G. Holmes; appellants' reply brief is due 6/7/89 for Securities Investor. [89-55094] (jhc) [89-55094]

02/16/89	Filed certificate of record on appeal Reporters Transcript filed in District Court N/T. [89-55094] (cck) [89-55094]
08/04/89	Filed original and 15 copies Appellant Securities Investor in 89-55094, Appellant Laurance A. Schroeder in 89-55128, Appellant Eugene W. Bell in 89-55128 Joint opening brief 50 pages, and five excerpts of record in 1 volume; served on 8/1/89 [89-55094, 89-55128] (jw) [89-55094, 55128]
08/04/89	Filed original and 15 copies Trustee's separate opening brief 20 pages, served on 8/1/89 [89-55094, 89-55128] (jw) [89-55094, 89-55128]
08/09/89	Filed SEC in 89-55094, SEC in 89-55128's motion for leave to file a brief, Amicus Curiae, out of time, (PROMO to CONFATT); served on 8/8/89 [1643832] [89-55094, 89-55128] (jw) [89-55094, 89-55128]
09/06/89	Filed order (NOONAN): The motion to file a brief, amicus curiae, late is granted. The brief received by the court shall be filed. Apellees motion for an enlargement of brief length is denied. [1643832-1] in 89-55094, 89-55128 [89-55094, 89-55128] (jw) [89-55094, 89-55128]

09/06/89	Filed original and 15 copies SEC in 89-55094, SEC in 89-55128's amicus brief of 15 pages; served on 8/8/89, previously received. [89-55094, 89-55128] (jw) [89-55094 89-55128]
10/05/89	Filed original and 15 copies appellee Robert G. Holmes in 89-55094, Robert G. Holmes in 89-55128's 75 pages brief, served on 10/3/89 [89-55094, 89-55128] (jw) [89-55094 89-55128]
10/27/89	Filed original and 14 copies Securities Investor in 89-55094 reply brief, 36 pages, served on 10/20/89 [89-55094, 89-55128] (ec) [89-55094 89-55128]
01/25/90	CALENDARED: PASADENA, MARCH 5, 1990 1:30 p.m. Courtroom 3 [89-55094, 89-55128] Case will now be heard on 3/6/90. (aw) [89-55094 89-55128]
03/06/90	ARGUED AND SUBMITTED TO: SCHROEDER, THOMPSON, TROTT [89-55094, 89-55128] (jhc) [89-55094 89-55128]

03/20/90	Filed order (SCHROEDER, THOMPSON, TROTT,): Securities Investor Protection Corporation and trustees Eugene W. Bell and Laurence A. Schroeder are hereby ordered to file within ten days of the date of this order supplemental excerpts of record to consist of the following documents: (1) pltfs'/Aplts' Statement of Background and Facts (clerk's record 1317); (2) Declaration of James C. Foley (clerk's record 1310); and (3) Declaration of John B. Torkelson (clerk's record 1309) [89-55094, 89-55128] (dmd) [89-55094 89-55128]
03/29/90	Filed 5 copies of Appellant Securities Investor in 89-55094 supplemental excerpts of record on appeal in 1 volumes, per order of 3/20/90, (PANEL) (jw) [89-55094 89-55128]
03/30/90	FILED, AS OF 2/16/89, CERTIFIED RECORD ON APPEAL IN 4 VOLS. (TOTAL): 4 CLERKS RECORDS (ORIG) [89-55094] [89-55094] (jw) [89-55094]
08/03/90	FILED OPINION: REVERSED REMANDED (Terminated on the Merits after Oral Hearing; Reversed; Written, Signed, Published. SCHROEDER; THOMPSON, author; TROTT.) FILED AND ENTERED JUDGMENT. [89-55094, 89-55128] (ck) [89-55094 89-55128]

09/25/90	MANDATE ISSUED to include costs. [89-55094, 89-55128] (jw) [89-55094 89-55128]
11/09/90	Received notice from Supreme Court: petition for certiorari filed Supreme Court No. 90-727 filed on 11/1/90. [89-55094] (dmd) [89-55094]

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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR PROTECTION CORPORATION, et al.,	)	CASE NO. 83-4742-AWT (Tx)
Plaintiffs,	)	FIRST AMENDED COMPLAINT FOR DAMAGES:
vs.	)	

SEYMOUR VIGMAN, AERO SYSTEMS, INC., AEROSONIC CORPORATION, CREDITBANK, INC., DASH INDUSTRIES, INC., HABERICO, INC., HABERS, INC., HABERS, INC., DEFINED BENEFIT PENSION TRUST, IBEBAFIN, S.A., KEOPS, S.A., MAGNETIC TECHNOLOGIES CORPORATION, TALINGO CORPORATION, TULA CORPORATION, MARTIN BLUMENTHAL, JOSE LUIS CALOGNE, aka JOSE LUIS CALONGE RIVAS, DOLORES OWENS CIPPARONE, aka DEE CIPPARONE, JAY DASH, PHILLIP DASH, ISADORE DIAMOND, ELLIOT I. EISEMAN, HERBERT J. FRANK, FRANKIE MAE GARRITY, RODGER W. GARRITY, DAVID S. GOLDMAN, JACK A. HABER, ROBERT G. HOLMES, JR., JOSEPH A. LUGO, JR., ROBERT J. MANSELL, GORDON H. McNEIL, EDWARD P. PRESCOTT, JOSE CAMPRUBI SALA, VELMA SHAW, aka VELMA SHAW MYERS, NETTIE VIGMAN and LAWRENCE WEST, aka LARRY WEST,

Defendants.

A) FOR VIOLATION OF THE SECURITIES EXCHANGE ACT OF 1934 [15 U.S.C. §§ 78a, *et seq.*];

B) FOR VIOLATION OF THE RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS ACT [18 U.S.C. §§ 1961, *et seq.*];

C) BREACH OF FIDUCIARY DUTY; and

D) FRAUD.

DEMAND FOR JURY TRIAL

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FIRST AMENDED COMPLAINT

Plaintiffs Securities Investor Protection Corporation; Eugene W. Bell, Trustee for the liquidation of Joseph Sebag Incorporated; and John L. Britton, Trustee for the liquidation of First State Securities Corporation allege as follows:[1]

JURISDICTION

1. This Court has jurisdiction over the subject matter of this action and the defendants named herein under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961, *et seq.*, ("RICO"), the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a, *et seq.*, (the "Exchange Act") and 28 U.S.C. § 1331. This Court further has jurisdiction over all state and common law claims asserted herein by virtue of its pendant jurisdiction in that such claims arise from a common nucleus of operative fact.

VENUE

2. Venue of this action lies in the Central District of California by virtue of 18 U.S.C. § 1965 and 15 U.S.C. § 78aa. Each defendant sued herein committed the statutory and/or common law violations alleged in this First Amended Complaint by the use of means or

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[1] This First Amended Complaint is filed pursuant to this Court's Memorandum Order on Motions to Dismiss entered May 30, 1984. The amendments made in compliance with that Order are without prejudice to all plaintiff's rights of appeal.

instrumentalities of interstate commerce or of the mails, or of facilities of the over-the-counter securities market, and

A. committed acts or engaged in the transactions constituting the violations in the Central District of California; or

B. at all relevant times was found, or is an inhabitant or a resident or transacts his (her) affairs in the Central District of California; or

C. the ends of justice require that the action be defended in this Court.

3. PARTIES PLAINTIFF

A. Securities Investor Protection Corporation.

Plaintiff Securities Investor Protection Corporation ("SIPC") is non-profit corporation created by the Securities Investor Protection Act of 1970, 15 U.S.C. § 78aaa, *et seq.* ("SIPA"). SIPC's members consist of broker-dealers registered under the Securities Exchange Act of 1934. SIPA specifically authorizes SIPC "to sue and be sued, complain and defend, in its corporate name and through its own counsel, in any state, Federal, or other court." 15 U.S.C. § 78ccc(b)(1). In addition to the powers conferred under SIPA, SIPC has the powers of a non-profit corporation conferred by the District of Columbia non-profit corporations code. 6 D.C. Code § 29-501, *et seq.* (1981). To protect customers of securities broker-dealers from losses resulting from the financial failure of the broker-dealers,

SIPA empowers SIPC to commence liquidation proceedings in a United States District Court when SIPC determines that the broker-dealer has failed or is in danger of failing to meet its obligations to its customers and one or more of four specific conditions, including failure to maintain net capital at statutorily-required levels, exists.

B. Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag, Incorporated.

Joseph Sebag Incorporated, was a Delaware corporation doing business in interstate commerce as a securities broker-dealer registered with and licensed by the National Association of Securities Dealers ("NASD") with its principal place of business in Los Angeles, California. Joseph Sebag Incorporated, owned all the outstanding stock of Investors Financial Services, Inc. ("IFS"), which had offices located in Los Angeles and Irvine, California, and carried all customer accounts on behalf of IFS on a fully disclosed basis. Like Joseph Sebag Incorporated, IFS was also engaged in interstate commerce as a securities broker-dealer. In July, 1981, and at various periods during the preceding five years, Joseph Sebag Incorporated, and IFS (hereinafter collectively referred to as "Sebag") traded on behalf of its customers and for Sebag's own account the following over-the-counter ("OTC") securities, among others: Aerosonics Corporation ("Aerosonics"), Aero Systems, Inc. ("Aero Systems"), Bunnington Corporation ("Bunnington"), Creditbank, Inc. ("Creditbank"), Dash Industries, Inc. ("Dash"), Intercontinental Diamond Corporation ("Intercontinental Diamond") and Osrow Products Corporation ("Osrow

Products"). All of these issuers were themselves engaged in interstate commerce.

On July 27, 1981, Eugene W. Bell ("Bell") was, upon application by SIPC and a finding that the customers of Sebag were in the need of the protection afforded by SIPA, appointed trustee for the liquidation of Sebag by the Honorable Malcolm M. Lucas, Judge of the United States District Court for the Central District of California. At all times subsequent to July 27, 1981, Bell has been the duly qualified and acting trustee for the liquidation of Sebag possessing all of the rights and remedies afforded a trustee under SIPA and those sections of the Bankruptcy Code (11 U.S.C. § 101, *et seq.*) not inconsistent with SIPA.

C. John L. Britton, Trustee for the Liquidation of First State Securities Corporation.

First State Securities Corporation ("FSSC") was a Delaware corporation engaged in interstate commerce as a securities broker-dealer with its principal place of business in North Miami, Florida. In July 1981, and at various periods during the preceding five years FSSC traded the following issues, among others, on behalf of its customers and for its own account: Aerosonic, Aero Systems, Bunnington, California Leisure Products, Inc. ("California Leisure"), Creditbank, Dash and Osrow Products.

On July 24, 1981, John L. Britton ("Britton") was, upon application by SIPC and a finding that the customers of FSSC were in need of the protection afforded by SIPA, appointed trustee for the liquidation of FSSC by the Honorable James Laurence King, Judge of the United States District Court for the Southern District of Florida.

At all times subsequent to July 24, 1981, Britton has been the duly qualified and acting trustee for the liquidation of FSSC possessing all of the rights and remedies afforded a trustee under SIPA and those sections of the Bankruptcy Code (11 U.S.C. §101, *et seq.*) not inconsistent with SIPA.

4. Pursuant to SIPC's statutory obligations to advance funds needed to satisfy net equity claims of the customers of Sebag and FSSC and to advance funds for costs and expenses of administration, SIPC has paid in excess of the following sums in the liquidation proceedings to date:

Sebag – $12,020,877

FSSC – $ 895,790.

SIPC continues to pay such sums as are appropriate under its statutory authority. SIPC will amend this First Amended Complaint at the time of trial to show all such sums paid.

PARTIES DEFENDANT

5. The defendants are as follows:

A. *Rico Defendants*:[2] The following defendants planned, conducted or knowingly participated in the conspiratorial pattern of racketeering activity involving the fraudulent manipulation of the market prices of the over-the-counter securities hereinafter alleged:

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[2] Defendants against whom plaintiffs assert claims for relief under the RICO Act, 18 U.S.C. §§ 1961, *et seq.*

(1) Corporate RICO Defendants:

Aero Systems, Inc. ("Aero Systems")

Second, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Robert G. Holmes, Officer and Director.

Aerosonic Corporation ("Aerosonic")

First, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Herbert J. Frank and David S. Goldman, Officers and Directors.

Creditbank, Inc. ("Creditbank")

Fourth, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Jose Luis Calonge, aka Jose Luis Calonge Rivas, Jose Camprubi Sala, Joseph A. Lugo, Jack A. Haber, Directors.

Dash Industries, Inc. ("Dash")

Fifth, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Martin Blumenthal, Jay Dash, Phillip Dash, Officers and Directors.

Ibebafin, S.A.

Fourth and Seventeenth Claims for Relief.

Keops, S.A.

Fourth and Seventeenth Claims for Relief.

Magnetic Technologies Corporation [formerly known as Bunnington Corporation ("Bunnington")]

Third, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Isadore Diamond (Chairman

of the Board); Seymour Vigman, Gordon H. McNeil, Officers and Directors.

Talingo Corporation (Talingo")

First, Third, Fourth, Sixth and Seventeenth Claims for Relief.

Tula Corporation ("Tula")

First, Third, Fourth, Sixth and Seventeenth Claims for Relief.

(2) Individual RICO defendants who are residents of the Central District of California:

Garrity, Frankie Mae

Eleventh and Seventeenth Claims for Relief – wife of defendant Garrity, registered principal of IFS; maintained securities accounts at Sebag.

Garrity, Rodger W. ("Garrity")

First through Sixth, Seventeenth, Eighteenth and Nineteenth Claims for Relief – husband of defendant Frankie Mae Garrity, registered representative of IFS.

Vigman, Nettie

Tenth and Seventeenth Claims for Relief – wife of defendant Seymour Vigman, sister of defendant Isadore Diamond; maintained securities accounts at Sebag and FSSC.

Vigman, Seymour ("Vigman")

First, Second, Third, Fifth, Sixth, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Officer, shareholder and Chairman of the Executive Committee of defendant Bunnington, a "controlling person" of Bunnington within the meaning of 15 U.S.C. §§ 77o and 78t; husband of defendant Nettie Vigman; brother-in-law of defendant Isadore Diamond.

(3) Individual RICO defendants who transacted their affairs within the Central District of California at all relevant times herein:

Frank, Herbert J. ("Frank")

First, Sixteenth, Seventeenth and Nineteenth Claims for Relief – President, Chairman of the Board of Directors; "controlling person" of defendant Aerosonic.

Holmes, Robert G., Jr. ("Holmes")

Second, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Officer, Director and "controlling person" of defendant Aero Systems, Inc.

Lugo, Joseph A., Jr. ("Lugo")

First through Sixth, Seventeenth, Eighteenth and Nineteenth Claims for Relief – Officer, Director, shareholder and registered principal of FSSC; Director and "controlling person" of defendant Creditbank.

Shaw, Velma (aka Velma Shaw Myers) ("Shaw")

First, Second, Third, Fifth, Sixth, Seventeenth, Eighteenth and Nineteenth Claims for Relief – registered principal of IFS; resident of the Central District of California.

(4) Individual RICO defendants who knowingly assisted, participated or conspired with other defendants in the consummation of the fraudulent, manipulative scheme hereinafter alleged:

Blumenthal, Martin ("Blumenthal")

Fifth, Seventeenth and Nineteenth Claims for Relief – Officer, Director, "controlling person" and shareholder of Dash Industries, Inc.; maintained securities accounts at FSSC.

Calonge, Jose Luis [aka Jose Luis Calonge Rivas] ("Calonge")

Fourth, Seventeenth and Nineteenth Claims for Relief – Chairman of the Board of Directors, majority shareholder and "controlling person" of defendant Creditbank; maintained securities accounts at FSSC; Officer and "controlling person" of JLC CIA Inversionista, S.A.; and "controlling person" of Mobile International Corporation.

Cipparone, Dolores Owens (aka Dee Cipparone) ("Cipparone")

Seventh, Seventeenth and Eighteenth Claims for Relief – registered principal, Officer, Director, shareholder and "controlling person" of FSSC; maintained securities account at FSSC.

Dash, Jay

Fifth, Sixteenth and Seventeenth Claims for Relief – Officer, Director, shareholder and "controlling person" of Dash Industries, Inc.; maintained securities accounts at FSSC.

Dash, Phillip

Fifth, Sixteenth and Seventeenth Claims for Relief – Officer, Director, shareholder and "controlling person" of Dash Industries, Inc.; maintained securities accounts at FSSC.

Diamond, Isadore ("Diamond")

Second, Third, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Chairman of the Board of Directors and a "controlling person" of defendant Bunnington; at one material time Director of defendant Aero Systems; brother of defendant Nettie Vigman; brother-in-law of defendant Vigman; maintained securities accounts at FSSC.

Eiseman, Elliot I. ("Eiseman")

Ninth, Seventeenth, Eighteenth and Nineteenth Claims for Relief – Officer, Director, shareholder, "controlling person" and registered principal of FSSC.

Goldman, David S.

First, Sixteenth, Seventeenth and Nineteenth Claims for Relief – Officer, Director and "controlling person" of Aerosonic; maintained securities accounts at Sebag and FSSC.

Haber, Jack A. ("Haber")

Fourth, Fifteenth, Sixteenth and Seventeenth Claims for Relief – Director and "controlling person" of Creditbank; Officer and "controlling person" of Habers, Inc., and Haberico, Inc.; maintained and/or controlled securities accounts at Sebag and FSSC.

McNeil, Gordon H. ("McNeil")

Third, Sixteenth, Seventeenth and Nineteenth Claims for Relief – President, Director and "controlling person" of defendant Bunnington.

Sala, Jose Camprubi ("Sala")

Fourth, Fourteenth, Sixteenth and Seventeenth Claims for Relief – honorary Chairman of the Board and "controlling person" of defendant Creditbank; maintained securities account at FSSC.

B. *Other Defendants:* The following defendants knowingly participated or aided and abetted in manipulating one or more of the securities as hereinafter alleged more particularly in plaintiffs' specific Claims for Relief:

(1) Corporate Defendants:

Haberico, Inc. ("Haberico")

Fifteenth Claim for Relief – maintained securities accounts at FSSC and Sebag; wholly-owned by Jack A. Haber; controlled by defendant Jack A. Haber.

Habers, Inc.,

Fifteenth Claim for Relief – Jack A. Haber, Officer.

Habers, Inc., Defined Benefit Pension Trust

Fifteenth Claim for Relief – maintained securities accounts at FSSC; accounts controlled by Jack A. Haber.

(2) Individual Defendants:

Mansell, Robert J. ("Mansell")

Eighth Claim for Relief – FSSC margin clerk.

Prescott, Edward P. ("Prescott")

Thirteenth and Eighteenth Claims for Relief – Officer, Chairman of the Board of Directors, "controlling person" and registered principal of Sebag; resident of the Central District of California.

West, Lawrence (aka Larry West) ("West")

Twelfth Claim for Relief – resident of the Central District of California; maintained securities accounts at Sebag and FSSC.

BACKGROUND OF THE RACKETEERING ENTERPRISE

6. The defendants, through acts, transactions and practices hereinafter described, using means or instrumentalities of interstate commerce including the mails, telephones, wires, broker-dealers and the facilities of over-the-counter securities markets, carried out an ongoing pattern of concerted activity to manipulate and artificially inflate the prices of various over-the-counter securities of corporations engaged in interstate commerce in which numerous defendants held large positions. The purpose, in part, of the manipulative conduct hereinafter alleged was to artificially inflate the prices of these securities so that the defendants could reap substantial illicit profits from the purchase, sale and repurchase of the securities on the OTC market, re-invest the proceeds from their sales in other entities engaged in interstate commerce, acquire interests in entities engaged in interstate commerce and induce others to purchase these securities.

7. The "manipulative scheme," began in or about June, 1964, and continued by the associations and acts hereinafter alleged through commencement of the liquidation proceedings of Sebag and FSSC in July, 1981. It was carried out by the concerted actions of issuer corporations, certain of their officers and directors, registered broker-dealers, registered representatives and employees of broker-dealers, securities traders and participating investors. Eventually, the fraudulent manipulations of the following OTC securities caused the net capital of Sebag and FSSC to fall below statutorily-required levels, thereby exposing their customers and SIPC to substantial risks and requiring that trustees be appointed to liquidate Sebag and FSSC under the provisions of SIPA:

Aero Systems;

Aerosonic;

Bunnington (presently Magnetic Technologies);

Creditbank;

Dash Industries; and

Osrow Products.

* * *

SECOND CLAIM FOR RELIEF BY PLAINTIFFS AGAINST DEFENDANTS AERO SYSTEMS, LUGO, GARRITY, SHAW, HOLMES, VIGMAN, AND DIAMOND

(Securities Fraud)

[17 C.F.R. § 240.10b-5; 15 U.S.C. § 78j(b)]

75. Plaintiffs incorporate herein by reference paragraphs 1 through 74 of this First Amended Complaint.

76. At all times relevant herein, defendant Homes was an officer, controlling person, within the meaning of 15 U.S.C. §§ 77o and 78t, principal shareholder and director of defendant Aero Systems. Defendant Diamond was, at relevant times herein, an officer, director, shareholder and controlling person of Aero Systems. Aero Systems at all times relevant transacted its affairs within the Central District of California. Defendant Diamond was also, at all times relevant herein, an officer, director and controlling person, within the meaning of 15 U.S.C. §§ 77o and 78t, of defendant Bunnington. All of these defendants owed a duty to the shareholders and purchasers and sellers of these companies' securities and the investing public to refrain from the conduct herein alleged.

77. As alleged above, defendant Aero Systems acquired DCS Financial and DCS Financial's subsidiary Springwater Manufacturing in July, 1976. On or about March 1, 1978, Aero Systems transferred Springwater Manufacturing to Honeoye Industries, Inc., a wholly-owned subsidiary of defendant Bunnington for $250,000 cash and the transfer to Aero Systems of a $350,000 note receivable.

78. Aero Systems included the operations of Springwater Manufacturing in Aero Systems' consolidated

statement of income for the fiscal year ended February 28, 1977, from the date of its acquisition effective July, 1976. Springwater Manufacturing's sales of $690,863 represented 14% of the reported total sales and operating revenue of Aero Systems for the fiscal year; and Springwater Manufacturing's income before income taxes of $46,803 was 47% of Aero Systems' consolidated income before income taxes and extraordinary credit for the fiscal year.

79. As alleged above, Aero Systems transferred Springwater Manufacturing to a Bunnington subsidiary in 1978, allowing Aero Systems to report a gain, in the fiscal year ended February 28, 1979, of $442,346 including income tax benefits. This gain represented 34% of Aero Systems' consolidated net income for that fiscal year.

80. The Aero Systems consolidated statement of income for the fiscal year ended February 28, 1978, reflected the impending sale of Springwater Manufacturing to Bunnington and reported the operations of Springwater Manufacturing on a single line as income from discontinued operations of $100,610 and $18,578 for the fiscal years ended February 28, 1978 and 1977, respectively. These figures represented 35% and 35.3%, respectively, of the income before extraordinary credit in each year.

81. If Aero Systems had not transferred Springwater Manufacturing to Bunnington effective March 1, 1978, and had not reported the operations of Springwater Manufacturing on one line as discontinued operations, sales and operating revenue for the fiscal year ending February

28, 1978, would have been reported as $7,932,038, including $1,609,823 of Springwater Manufacturing's sales. Springwater Manufacturing's sales would have accounted for 20.3% of Aero Systems' total pro-forma revenues.

82. Based on the facts alleged in paragraphs 76 through 81, above, plaintiffs allege that the motive, in part, for the acquisition by Aero Systems of DCS Financial (and its subsidiary, Springwater Manufacturing) was to permit Aero Systems to report improved financial performance with the intent to induce public confidence in and purchases of Aero Systems stock, to employ Aero Systems as a conduit to facilitate Bunnington's eventual acquisition of Springwater Manufacturing, and to place substantial positions of Aero Systems stock in the control of Speyer and defendants Nettie Vigman, McNeil, Blumenthal and Diamond.

83. In or about April, 1980, Aero Systems publicly announced that it had acquired from Colt Electronics Co., Inc. ("Colt Electronics") the exclusive marketing right to a computerized fuel management system for installation in commercial and private aircraft, known as the CD-3000 Fuel Management Computer ("CD-3000"). In conjunction with this acquisition, Aero Systems and Holmes made, or caused to be perpetuated, statements to the public and Aero System stockholders, including, among others, the following:

(a) An April 1, 1980, press release stating that "[t]he potential market for this much needed product includes all multi-engine jet, turbo prop and piston aircraft in the world. Robert G. Holmes, Jr., Aero's President stated

'We plan to market this fuel management computer thru our expanding world wide sales force and thru a selective network of dealers.' ";

(b) An April 23, 1980, press release stating that "Aero Systems plans to lease [the CD-3000] to commercial and business aircraft operators worldwide in exchange for a percentage of actual fuel savings. 'According to industry figures, the airlines alone will spend more than $30 billion for fuel this year,' Robert G. Holmes, Jr., Aero's president, noted.";

(c) A letter to shareholders, signed by defendant Holmes, in its 1980 Annual Report for its fiscal year ending February 29, 1980, stating that "We are very excited with our new 'Aero Systems Fuel Management Computer.' . . . Initial results from business jet users indicate fuel savings to be in the area of 10%. The market for this much needed product includes all multi-engine, turbo-prop and piston aircraft in the world.";

(d) A letter to shareholders, signed by defendant Holmes, in the 1981 Annual Report for fiscal year 1981 ending February 28, 1981, stating that "The excitement over our CD-3000 Fuel Management Computer continues to build as we get closer and closer to realizing its dramatic potential. We are now more convinced than ever about its success. The huge market for this unique new, high technology, energy saving device includes all multi-engine aircraft and helicopters in the world. . . . The CD-3000 has been installed in a variety of business jets and users estimate the fuel savings to be in the area of 10%. . . . In 1980 the major trunk airlines spent more than $30 billion for fuel . . . and the timing for introduction of our fuel saving computer couldn't be better.";

(e) Exxon *Aviation News*, October 24, 1980: "Aero Systems, Inc. is leasing an aircraft fuel

management computer from Colt Electronics to commercial and business aircraft operators worldwide in exchange for a percentage of actual fuel savings.";

(f) *Portfolio Letter*, Vol. II, no. 39, September 29, 1980, stating that "Aero President *Robert Holmes, Jr.*, told PL he had 400 'serious' prospects for the CD-3000. 'We stumbled across a new market for the CD-300[sic],' he added, explaining that the large helicopters that shuttle back and forth to off-shore oil rigs have very little in the way of cockpit-based fuel monitors."

(g) A Miami Herald article of September 29, 1980 quoting defendant Holmes: "We think this is a wonderful product for the times . . . Our tests show that it can result in fuel savings of up to 10 per cent."; and

(h) January 12, 1981, press release, signed by defendant Holmes, stating that "[t]he response to our unique new fuel saving computer has been excellent. Several airlines are on the verge of placing orders for the CD-3000 Fuel Management Computer and we have many pending orders from the business aircraft market."

These misleading statements to the public created an impression that sales of the computer had already been made, that large numbers of additional sales were imminent and that such sales would be profitable to Aero Systems. These statements were made with the intent, in part, of generating public interest in the Aero Systems stock and thereby inducing purchases of the stock.

84. At the time the statements were made, defendants Aero Systems and Holmes knew that the statements were false and misleading or were made in

reckless disregard of the truth, and that the statements omitted to include material facts necessary to make the statements not misleading in light of the circumstances under which they were made, in that:

(a) No sales of the CD-3000 had been made and there was no reasonable prospect of sufficient sales in the near future to yield the represented profits.

(b) The statements vastly overstated the potential market for this product. Rather than including all multi-engine aircraft in the world, the market was limited to only aircraft regularly used for flights of a certain duration and above a certain altitude.

(c) The statements created the false impression that Aero Systems would reap a bonanza consisting of a significant percentage of the $3 billion that trunk airlines would allegedly "save" using the CD-3000.

(d) There was no reasonable factual basis for the projected 10% fuel savings.

(e) Aero Systems failed to disclose that the agreement with Colt Electronics required an immediate payment of $100,000 to Colt Electronics and an additional immediate purchase by Aero Systems of $87,000 in equipment from Colt Electronics.

(f) Aero Systems failed to disclose that it was obligated to purchase $1,000,000 in equipment from Colt Electronics at the rate of $200,000 bi-annually as a condition precedent to retention of the rights to the CD-3000.

85. Beginning no later than September, 1980 and continuing through July, 1981, Aero Systems, acting

through defendant Holmes, also caused false or recklessly misleading material representations regarding the corporation's sales and projected earnings for fiscal year 1981 and future sales and earnings of the CD-3000 to be publicly disseminated or perpetuated through newspapers, periodicals and securities analysts. These knowing misrepresentations, intended to induce public confidence in and purchases of Aero Systems securities included, among others, the following:

> (a) Statements in Moore & Schley, Cameron & Co. Research Department publication, by Jules Augus, dated September 25, 1980, that Aero Systems' "area of greatest current excitement is the acquisition in April, 1980 of the worldwide marketing and distribution rights for a new aircraft fuel management computer system – the CD-3000. The system has indicated, in early testing, fuel savings in the area of 10%. This unique system's fuel savings could pay for the cost of the computer ($7,500 or more) on a business aircraft in three months and for a commercial jet installation in less than three weeks. This system . . . has a potential market of 50,000 private aircraft, 5,500 commercial aircraft, and for a large number of military aircraft . . . The Company is currently working on a foreign deal which could result in the sale of 250-400 units . . . The potential to Aero from this new high technology product could eventually provide greater revenues than from its current business alone.'";

(b) Statements in Wheat First Securities *Technology Group* publication, November 6, 1980, that Aero Systems would "achieve $20 million in sales for this year, with earnings per share of $0.27, and exceed the $50 million sales level within two years" and that the "CD-3000 is a

unique new energy saving device suitable for any jet or propeller aircraft, as well as helicopters.";

(c) Statements in undated Porter Le Vay & Rose, Inc. *Aero Systems, Inc. Information Report* that fiscal year 1981 sales would reach $20 million with earnings close to $.30 per share even without the impact of CD-3000 sales;

(d) Statements in Alan J. Wax column, New York Post, October 13, 1980, attributed to Jules Augus, that Aero Systems had made a significant number of sales of the CD-3000 including an order of 250 units by a foreign government; and

(e) Statements in Dick Davis' column, Miami Herald, November 16, 1980, attributed to Jules Augus, that the CD-3000 "can produce fuel savings of up to 10 per cent – savings that can pay for the cost of the computer in three weeks to three months, depending on the aircraft."

86. The above material misstatements and factual omissions were false and misleading for, among other things, the following reasons:

> (a) The statements misrepresented the interest of potential buyers in the CD-3000 and omitted to state that the prospective market for the CD-3000 was very limited.
>
> (b) There was no reasonable basis for the projected sales and future earnings and there was no reasonable basis for the projection that future sales would substantially add to the profitability of Aero Systems.
>
> (c) There was no reasonable factual basis for the estimated 10% fuel savings that purportedly could be achieved by users of the CD-3000.

(d) Aero Systems had not sold 250 units of the CD-3000 as of October, 1980.

87. Plaintiffs are informed and believe, based upon a December 9, 1982 Aero Systems press release, and thereon allege, that contrary to the above-alleged public pronouncements made by or at the direction of defendants Aero Systems and Holmes, Aero Systems made no sales of the CD-3000 until late 1982, when 2 sales were made.

88. In or about August, 1980, defendant Garrity traveled to Florida to confer with defendant Lugo. The market price of Aero Systems stock substantially increased thereafter from a price of $2 5/8 bid, $2 3/4 ask in August, 1980 to a price of $7 bid, $7 1/8 ask in September, 1980. Plaintiffs are informed and believe, and thereon allege, that the purpose of this meeting was to discuss the methods by which defendants Lugo and Garrity would effect the manipulation of that stock and thereby raise its price.

89. Plaintiffs are informed and believe, and thereon allege, that defendants Lugo, Garrity and Shaw, with knowledge of the above omissions and that the above material misstatements and misrepresentations were false or in reckless disregard of the truth, worked in concert with defendants Aero Systems, Holmes, Diamond, Vigman and Nettie Vigman to raise the price of the Aero Systems securities by employing these misrepresentations and omissions as an artifice to induce purchases of the Aero Systems securities by the customers of Sebag and FSSC and thereby generate trading volume and cause a corresponding increase in the price of these securities. These defendants failed to disclose to investors their

domination and control of the market for Aero Systems stock and their scheme to manipulate its price.

90. Defendants Lugo and Garrity also began, in the summer of 1980, to purchase large positions of Aero Systems stock for the proprietary accounts of Sebag and FSSC with the intent to dominate and control the market for that stock and thereby artificially raise its price. Lugo made such purchases from various of the participants in the racketeering enterprise, including but not limited to, purchases from Nettie Vigman and Diamond.

91. The above-alleged conduct by these defendants materially contributed to the net capital deficiencies of Sebag and FSSC by permitting defendants Lugo and Garrity to acquire large positions of Aero Systems common at inflated and manipulated prices and to pay out proceeds to defendants and others who sold the securities, directly or indirectly, through or to Sebag and FSSC. The defendants and others thereby extracted substantial capital from FSSC and Sebag and further contributed to their respective net capital deficits, depletion of the funds of customer property and the ultimate demise of Sebag and FSSC.

92. The conduct alleged herein constituted a fraud on the marketplace for Aero Systems common whereby the investing public, and the customers and creditors of Sebag and FSSC were unable to obtain true and accurate information concerning the legitimate demand for, supply of and resulting price of Aero Systems common.

93. As a result of the manipulation, the market price of Aero Systems stock continued to rise from the September, 1980 bid and ask prices to $9 3/8 bid, $9 1/2 ask in

early December, 1980. Thereafter, Aero Systems stock split five shares for four in January, 1981. The split stock reached a high of $7 5/8 bid, $7 7/8 ask on May 8, 1981, the equivalent of over $9 1/2 bid on a pre-stock-split basis. The bid price remained at $6 or more per share through June 29, 1981. Upon the demise of the manipulative scheme herein alleged, the price of the stock declined, dropping to $5 1/4 bid, $5 3/8 ask on July 27, 1981.

94. For the fiscal year ended February 28, 1979, Aero Systems had reported net income of $1,300,585, which included the gain of $442,346 from the sale of Springwater Manufacturing as alleged above. After retroactively reflecting the 5-for-4 stock split of January, 1981, the market price per share at bid, as of February 28, 1979, was $1.90 and net income per share was $0.21. The total market price at bid of Aero Systems stock outstanding was 3.27 times the net worth of the company which had a price (bid) earnings ratio of 9 to 1.

95. Net income for Aero Systems declined for the fiscal year ended February 29, 1980. After retroactively reflecting the January, 1981 stock split, net income per share dropped to $0.134 for fiscal year 1980, but the market price of the stock increased. The total market price for Aero Systems stock outstanding, as of February 29, 1980, increased to 4.12 times the net worth of Aero Systems, while the price to earnings ratio increased to 22.4 to 1.

96. For fiscal year 1981, ending February 28, 1981, net income continued to decline, as did net income per share which fell to $0.075. In spite of a price to earnings ratio of over 150 to 1, the continued manipulation of the price of Aero Systems common resulted in the total market price for

Aero Systems' outstanding stock increasing to in excess of 5.7 times the net worth of Aero Systems.

97. Between April, 1980 and July, 1981, defendants Nettie Vigman, Diamond, and Holmes, among others, with knowledge of the fraud perpetrated on the market by Aero Systems, Lugo and Garrity as herein alleged, sold large positions of Aero Systems stock at artificially inflated prices. Such sales include, but are not limited to:

(a) Diamond's sale of 25,000 shares of Aero Systems at $4 per share on or about September 18, 1980, for proceeds of $100,000; 25,000 shares at $4 1/4 per share on or about September 19, 1980, for proceeds of $106,250; and plaintiffs are informed and believe, and thereon allege, that defendant Diamond sold 7,908 shares of Aero Systems on or about February 19, 1981, for proceeds of $41,517;

(b) Nettie Vigman's sales of Aero Systems stock;

Quantity	Approximate Date	Price	Proceeds
10,000	September 4, 1980	$3 5/8	$ 36,250
10,000	September 4, 1980	$3 1/2	$ 35,000
35,000	April 2, 1981	$5 3/4	$ 201,250
7,500	April 6, 1981	$6	$ 45,000
10,000	April 7, 1981	$5 7/8	$ 58,750
12,500	April 7, 1981	$5 7/8	$ 73,437.50
25,000	April 13, 1981	$6 5/8	$ 165,625
35,000	April 13, 1981	$6 1/2	$ 227,500
10,000	April 14, 1981	$6 5/8	$ 66,250
5,000	April 23, 1981	$6 5/8	$ 33,125
10,000	May 14, 1981	$6 3/4	$ 67,500
15,000	May 14, 1981	$6 1/4	$ 93,750
10,000	May 14, 1981	$7	$ 70,000
6,565	May 14, 1981	$7 1/8	$ 46,775.63
Total 201,565 shares			$1,220,213.13

(c) Plaintiffs are informed and believe, and thereon allege, that defendant Holmes sold 50,000 shares of Aero Systems stock at $8 per share on or about November 12, 1980, for proceeds of $400,000; and sold 25,000 shares at $5 per share on or about July 24, 1981, for proceeds of $125,000; and

(d) Sales by Speyer, the son-in-law of defendants Vigman and Nettie Vigman, of 50,000 shares of Aero Systems at $4¾ per share on or about September 23, 1980, for proceeds of $237,500; 45,698 shares of Aero Systems at $8½ per share on or about January 2, 1981, for proceeds of $388,433; and 11,227 shares of Aero Systems at $8 per share on or about January 9, 1981, for proceeds of $89,816. Plaintiffs are informed and believe, and thereon allege, that these transactions constituted all of the Aero Systems stock received by Speyer as a result of the acquisition of DCS Financial by Aero Systems, as alleged above.

98. As a direct and proximate result of the conduct alleged herein, plaintiffs have been damaged in a total amount not yet ascertained but exceeding $15,000,000. Plaintiffs will seek leave to amend this First Amended Complaint when their exact damages have been determined.

* * *

SIXTEENTH CLAIM FOR RELIEF BY PLAINTIFFS AGAINST DEFENDANTS AERO SYSTEMS; AEROSONIC; CREDITBANK; DASH; BUNNINGTON; HOLMES; FRANK; DAVID S. GOLDMAN; BLUMENTHAL; JAY DASH; SALA; HABER; PHILLIP DASH; DIAMOND; VIGMAN; McNEIL

[Aiding and Abetting Violations of 17 C.F.R. § 240.10b-5; 15 U.S.C. § 78j(b)]

239. Plaintiffs incorporate by reference paragraphs 1 through 238 of this First Amended Complaint.

240. At all times relevant herein and in particular during the period that Lugo, Garrity and Shaw were engaged in the fraudulent, manipulative conduct herein alleged:

(a) Defendants Holmes and Aero Systems were aware of the true financial condition of Aero Systems;

(b) Defendants Frank, David S. Goldman and Aerosonic were aware of the true financial condition of Aerosonic;

(c) Defendants Haber, Sala and Creditbank were aware of the true financial condition of Creditbank;

(d) Defendants Blumenthal, Jay Dash, Phillip Dash and Dash were aware of the true financial condition of Dash;

(e) Defendants Diamond, Vigman, McNeil and Bunnington were aware of the true financial condition of Bunnington; and

(f) Each of the above-captioned defendants knew that FSSC and Sebag traded substantial positions in the securities of their respective corporations: (1) for the proprietary accounts of

FSSC and Sebag; and (2) for the customer accounts of FSSC and Sebag.

241. Plaintiffs are informed and believe, and therefore allege, that the above-captioned defendants knew or recklessly disregarded information available to them that indicated that the price of their respective corporation's common stock bore no reasonable relationship to its true financial condition.

242. The above-captioned defendants substantially assisted Lugo, Garrity and Shaw to fraudulently manipulate the prices of the securities of the above-captioned corporations by:

(a) Issuing or causing to be issued false and misleading statements contained in press releases, letters, advertising, public statements and other media concerning their respective corporate financial conditions, new products and acquisitions as previously alleged herein to the general public, to their shareholders and to defendants Lugo, Garrity and Shaw;

(b) Consummating several mergers and acquisitions during the period that Lugo, Garrity and Shaw engaged in their fraudulent manipulations; and

(c) Defendants Aerosonic, Dash and Bunnington made various private placements of their securities during the period that Lugo, Garrity and Shaw engaged in their fraudulent manipulations.

All of the above-referenced conduct was done with the intent to induce public confidence in purchases and OTC market activity in the respective securities of the above-captioned corporate defendants.

243. An integral part of the various manipulations herein alleged was the creation of public interest in, and purchases of, the securities of the above-captioned corporations through the public dissemination of misleading information regarding their financial status, purported products, mergers and acquisitions and private placements.

244. Plaintiffs are informed and believe, and therefore allege, that the above-captioned individual defendants had actual knowledge of defendants Lugo, Garrity and Shaw's fraudulent manipulation of the price for the common stock of the corporations of which those individual defendants were officers and/or directors and further had actual knowledge of their respective roles in those manipulations. Plaintiffs are informed and believe, and therefore allege, that the above-captioned corporate defendants, through their officers, directors or agents, also had actual knowledge of those manipulations and the respective roles of those corporate defendants therein.

245. As a direct and proximate result of the conduct alleged herein, plaintiffs have been damaged in a total amount not yet ascertained, but exceeding $15,000,000. Plaintiffs will seek leave to amend this First Amended Complaint when their exact damages have been determined.

SEVENTEENTH CLAIM FOR RELIEF BY PLAINTIFFS AGAINST THE FOLLOWING DEFENDANTS: DIAMOND; EISEMAN; VIGMAN; NETTIE VIGMAN; LUGO; GARRITY; FRANKIE MAE GARRITY; HOLMES; AERO SYSTEMS; BLUMENTHAL; PHILLIP DASH; JAY DASH; DASH; HABER; SALA; CALONGE; CREDITBANK; IBEBAFIN, S.A.; KEOPS, S.A.; McNEIL; BUNNINGTON; AEROSONIC; DAVID S. GOLDMAN; FRANK; CIPPARONE; SHAW; TALINGO; AND TULA; COLLECTIVELY REFERRED TO IN THIS CLAIM AS THE "RICO DEFENDANTS."

(RICO Violations)

[18 U.S.C. § 1961, et seq.]

246. Plaintiffs incorporate herein by reference paragraphs 1 through 245 of this First Amended Complaint.

247. From as early as 1964 and continuing to the date hereof, the RICO Defendants, and each of them: (1) have received income from a pattern of racketeering activity and have used and invested such income to acquire interests in, establish and operate an enterprise engaged in and affecting interstate commerce (the "racketeering enterprises"); (2) have, through a pattern of racketeering activity, acquired and maintained interest in and control of the racketeering enterprise; (3) have, through their employment by or association with the racketeering enterprise, conducted and participated in the conduct of the affairs of the racketeering enterprise; and (4) have conspired among themselves to accomplish the above as herein alleged. Between no later than January, 1979 and continuing through at least July, 1981 the RICO defendants continued to carry on the racketeering enterprise through FSSC and Sebag. This conduct gave the RICO

defendants two additional access points to the OTC market that facilitated the pattern of racketeering activity herein alleged.

248. Plaintiffs are informed and believe and thereon allege that, in the course of the above-described racketeering activity, the RICO Defendants, and each of them committed fraud in the sale of securities, violated Sections 1341 and 1343 of Title 18, United States Code (mail and wire fraud, respectively) and committed offenses involving fraud connected with a case under Title 11, United States Code. In the course of the pattern of racketeering activity alleged herein, the RICO Defendants, and each of them committed at least two acts of racketeering activity, as defined in 18 U.S.C. § 1961(1), within ten years of each other.

249. The Aerosonic manipulation (First Claim For Relief), the Aero Systems manipulation (Second Claim For Relief), the Bunnington manipulation (Third Claim For Relief), the Creditbank manipulation (Fourth Claim For Relief), the Dash manipulation (Fifth Claim For Relief), and the Osrow Products manipulation (Sixth Claim For Relief) were in fact a series of interdependent, consciously parallel courses of conduct engaged in pursuant to a tacit understanding between the RICO defendants and constituted a conspiracy by the RICO defendants to do the acts alleged herein.

250. The activity alleged herein permitted the RICO Defendants, and each of them, to maintain an anticompetitive and favored position in the national OTC market vis-a-vis the general public, and resulted in extensive

financial loss to SIPC and the securities account customers of FSSC, and Sebag. Such racketeering activity also resulted in anti-competitive control and domination by the RICO Defendants over Sebag and FSSC, resulting in financial destruction and the liquidation of Sebag and FSSC and damages to SIPC.

251. The conduct alleged in paragraphs 1 through 250, inclusive, constitutes violations of 18 U.S.C. § 1962.

252. Pursuant to 18 U.S.C. 1964(c), plaintiffs are entitled to treble the damages proved at trial. Further, plaintiffs are entitled to such injunctive and equitable relief provided for under 18 U.S.C. § 1964(a), as the Court may deem just and proper.

253. Pursuant to 18 U.S.C. § 1964(c), plaintiffs are entitled to recover their costs of suit and reasonable attorneys' fees.

254. As a direct and proximate result of the conduct alleged herein, plaintiffs have been damaged in a total amount not yet ascertained but exceeding $15,000,000. Plaintiffs will seek leave to amend this First Amended Complaint when their exact damages have been determined.

* * *

WHEREFORE, plaintiffs pray for relief as follows:

A. By Plaintiff SIPC:

1. For damages in the amount of all advances to the respective trustees for payment of net equity claims paid

to customers of FSSC and Sebag since commencement of their liquidation proceedings according to proof;

2. For damages to that portion of the fund of customer property to which SIPC is subordinated to the claims of customers of FSSC and Sebag according to proof;

3. For all advances for costs and expenses of the administration of the liquidation proceedings of Sebag and FSSC according to proof;

4. For treble the damages referenced in paragraphs 1, 2 and 3 of this Prayer;

5. For punitive damages in the amount of $100,000,000; and

6. For reasonable attorneys' fees and costs.

B. By Plaintiffs Bell and Britton:

7. For damages caused to that portion of the debtors' estates available to satisfy creditor claims, subordinated lenders and shareholders according to proof;

8. For destruction of the businesses of Sebag, FSSC and for loss of goodwill;

9. For all costs and expenses of their administration of the estates of Sebag and FSSC;

10. Treble the damages referenced in paragraphs 7, 8 and 9 of this Prayer;

11. Punitive damages in the amount of $100,000,000; and

12. For reasonable attorneys' fees and costs.

C. By All Plaintiffs:

13. For such equitable and injunctive relief as the Court deems proper.

14. For such other and further relief as the Court deems proper.

Dated: September 27, 1984.

JONES, BELL, SIMPSON & ABBOTT
C. EDWARD SIMPSON
ROBERT A. GRAHAM

By /s/ C. Edward Simpson
C. Edward Simpson
Attorneys for Plaintiffs
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John L. Britton, Trustee for
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State Securities Corporation

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JOHN A. STURGEON
ROY G. WUCHITECH

By /s/ Stephen C. Taylor
Stephen C. Taylor
Attorneys for Plaintiff
Securities Investor
Protection Corporation

DEMAND FOR JURY TRIAL

Pursuant to Fed.R.Civ.P. 38 (b), plaintiffs respectfully request trial by jury.

Dated: September 27, 1984.

JONES, BELL, SIMPSON & ABBOTT
C. EDWARD SIMPSON
ROBERT A. GRAHAM

By /s/ C. Edward Simpson
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DECLARATION OF SERVICE BY MAIL

[U. S. District Court, Central District, Local Rule 5(b)(3)]

SHARON L. STEVENSON, the undersigned, hereby declares

Declarant is a citizen of the United States and is employed by the law firm of Sheppard, Mullin, Richter & Hampton, 48th Floor, 333 South Hope Street, Los Angeles, California 90071. Declarant is over the age of 18 years and not a party to the within action. On September 27, 1984, at the direction of Stephen C. Taylor of said firm, and a member of the Bar of the United States District Court for the Central District of California, I served the within FIRST AMENDED COMPLAINT FOR DAMAGES: A) FOR VIOLATION OF THE SECURITIES EXCHANGE ACT OF 1934 [15 U.S.C. §§ 78a, *et seq.*]; B) FOR VIOLATION OF THE RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS ACT [18 U.S.C. §§ 1961, *et seq.*]; C) BREACH OF FIDUCIARY DUTY; and D) FRAUD. DEMAND FOR JURY TRIAL on the attorney(s) of record for the defendants in this matter by mailing, with postage thereon fully prepaid, in a mail facility regularly maintained by the United States Postal Service, a true copy thereof to said attorney(s) at their known address, to wit:

PLEASE SEE ATTACHED LIST

I declare under penalty of perjury that the foregoing [sic] is true and correct.

Executed at Los Angeles, California, on the 27th day of September, 1984.

/s/ Sharon L. Stevenson
Declarant

September 27, 1984

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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR PROTECTION CORPORATION, et al., **PLAINTIFF(S)** vs. SEYMOUR VIGMAN (please see attached) **DEFENDANT(S)**	)	CASE NUMBER CV-83-4742-AWT (Tx) SUMMONS ON FIRST AMENDED COMPLAINT

TO THE ABOVE-NAMED DEFENDANT(S), You are hereby summoned and required to serve upon

JONES, BELL, SIMPSON and & ABBOTT
Attorneys for Plaintiffs
Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated, and John L. Britton, Trustee for the Liquidation of First State Securities Corporation

SHEPPARD, MULLIN, RICHTER & HAMPTON
Attorneys for Plaintiff Securities Investor Protection Corporation

Plaintiff's attorney, whose address is:

Suite 580
800 Wilshire Boulevard
Los Angeles, California 90017

48th Floor
333 South Hope Street
Los Angeles, California 90071

an answer to the complaint which is herewith served upon you within 20 days after service of this summons upon you, exclusive of the day of service. If you fail to do so, judgment by default will be taken against you for the relief demanded in the complaint.

DATE: SEP 2, 1984

LEONARD A. BROSNAN, CLERK
By Yolanda Duron
Deputy Clerk
(SEAL OF THE COURT)

SUMMONS

SECURITIES INVESTOR PROTECTION CORPORATION, et al.,

Plaintiffs,

vs.

SEYMOUR VIGMAN, AERO SYSTEMS, INC., AEROSONIC CORPORATION, CREDITBANK, INC., DASH INDUSTRIES, INC., HABERICO, INC., HABERS, INC., HABERS, INC., [sic] DEFINED BENEFIT PENSION TRUST, IBEBAFIN, S.A., KEOPS, S.A., MAGNETIC TECHNOLOGIES CORPORATION, TALINGO CORPORATION, TULA CORPORATION, MARTIN

BLUMENTHAL, JOSE LUIS)
CALONGE, aka JOSE LUIS)
CALONGE RIVAS, DOLORES)
OWENS CIPPARONE, aka DEE)
CIPPARONE, JAY DASH, PHILLIP)
DASH, ISADORE DIAMOND,)
ELLIOT I. EISEMAN, HERBERT J.)
FRANK, FRANKIE MAE GARRITY)
RODGER W. GARRITY, DAVID S.)
GOLDMAN, JACK A. HABER,)
ROBERT G. HOLMES, JR., JOSEPH)
A. LUGO, JR., ROBERT J.)
MANSELL, GORDON H. McNEIL,)
EDWARD P. PRESCOTT, JOSE)
CAMPRUBI SALA, VELMA SHAW)
aka VELMA SHAW MYERS,)
NETTIE VIGMAN and)
LAWRENCE WEST, aka LARRY)
WEST,)
Defendants.)

---

* * *

BUCHALTER, NEMER, FIELDS,
CHRYSTIE & YOUNGER
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Attorneys for Defendant
Robert G. Holmes, Jr.

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

(FILED APR 3 - 1985)

SECURITIES INVESTOR PROTECTION CORPORATION, et al., Plaintiffs, vs. SEYMOUR VIGMAN, et al., Defendants.	CASE NO. 83-4742-AWT (Tx) ANSWER OF DEFENDANT ROBERT G. HOLMES, JR. TO FIRST AMENDED COMPLAINT FOR DAMAGES

Defendant Robert G. Holmes, Jr. ("Holmes") alleges as and as for his Answer to the First Amended Complaint for Damages (hereinafter the "Complaint") as follows:

1. Defendant Holmes denies that the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961, *et seq* ("RICO") is applicable to this action, and accordingly, defendant Holmes denies that this Court has jurisdiction over the subject matter of this action under

RICO as alleged in Paragraph 1 of the Complaint. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the remainder of the allegations contained in Paragraph 1 of the Complaint.

2. Defendant Holmes denies the material allegations contained in Paragraph 2 of the Complaint and expressly denies that venue of this action lies properly in the Central District of California.

3. Defendant Holmes admits the allegations contained in Paragraph 3(A) of the Complaint. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations set forth with respect to Joseph Sebag, Incorporated ("Sebag") in Paragraph 3(B) of the Complaint, except that defendant Holmes admits that at various times during the preceding five years, Sebag appeared to trade on behalf of certain of its customers the securities of defendant Aero Systems, Inc. (hereinafter "Aero Systems") and defendant Holmes admits that defendant Aero Systems was engaged in interstate commerce during the past five years. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 3(B) of the Complaint with respect to plaintiff Eugene W. Bell ("Bell"). Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained at Paragraph 3(C) of the Complaint with respect to plaintiff John L. Britain ("Britain") except that defendant Holmes admits that at certain times during the preceding five years First State Securities Corporation

("FSSC") appeared to trade the securities of Aero Systems for certain of its customers.

4. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 4 of the Complaint.

5. Defendant Holmes admits that the persons identified in Paragraph 5 of the Complaint appear to have been made defendants in this action. In all other respects, defendant Holmes denies the allegations of Paragraph 5 of the Complaint pertaining to defendants Holmes and Aero Systems and denies knowledge or information sufficient to form a belief as to the truth of these allegations insofar as they pertain to other named defendants.

6. Defendant Holmes denies the allegations contained in Paragraph 6 of the Complaint as applied to defendants Holmes and Aero Systems and, without limiting the generality of the foregoing, expressly denies that defendant Holmes engaged in any conduct to manipulate and artificially inflate the price of any security. With respect to all other defendants, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 6 of the Complaint.

7. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 7 of the Complaint except that defendant Holmes denies that there was any fraudulent manipulation of the common stock of Aero Systems with respect to which defendants Holmes or Aero Systems engaged in any wrongful conduct.

8. Defendant Holmes denies the allegations contained in Paragraph 8 of the Complaint as applied to defendant Holmes and denies knowledge or information sufficient to form a belief concerning the truth of such allegations as applied to other defendants.

9. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 9 of the Complaint.

10. Defendant Holmes denies the allegations of Paragraph 10 of the Complaint as applied to defendant Holmes and denies knowledge or information sufficient to form a belief concerning the truth of such allegations as applied to other defendants except that defendant Holmes admits that by means of a prospectus dated March 2, 1967, Aero Systems publicly offered 100,000 shares of its common stock in an offering with respect to which J.C. Roberts was an underwriter and otherwise upon terms and conditions more particularly described in such prospectus, the entirety of which is hereby incorporated by reference.

11. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 11 through 18, inclusive of the Complaint.

12. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations pertaining to exercise of control by Seymour Vigman ("Vigman") over corporations and issuers of securities referred to in Paragraph 19 of the Complaint except that defendant Holmes denies that Vigman exercised control over defendant Aero Systems.

Defendant Holmes admits that defendant Vigman provided certain financial advice to defendant Aero Systems and in all other respects, defendant Holmes denies the allegations contained in Paragraph 19 of the Complaint.

13. Defendant Holmes denies the allegations contained in Paragraph 20 of the Complaint as applied to defendant Holmes and denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they pertain to other defendants.

14. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 21 through 25, inclusive of the Complaint.

15. Defendant Holmes admits the allegations contained in Paragraph 26 of the Complaint.

16. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 27 of the Complaint.

17. Defendant Holmes admits the allegations contained in Paragraph 28 of the Complaint.

18. Defendant Holmes admits that on or about July 1976, a subsidiary of defendant Aero Systems acquired DCS Financial which was merged into Aero Systems Avionics, and in all other respects, defendant Holmes denies the allegations contained in Paragraph 29 of the Complaint and refers to and hereby incorporates by reference the full text of the acquisition agreement and publicly filed reports and disclosures of such agreement for an accurate description of the transaction.

19. Defendant Holmes denies that any purpose, in whole or in part, for the merger of DCS Financial into a subsidiary of Aero Systems was in any manner unlawful or improper, and in all respects defendant Holmes denies the allegations contained in Paragraph 30 of the Complaint.

20. Defendant Holmes denies that defendant Isadore Diamond ("Diamond") became an officer or director of Aero Systems in order to "assist" defendant Holmes; defendant Holmes admits that the individuals acquired the number of Aero Systems shares set forth in Paragraph 31, and in all other respects, defendant Holmes denies the allegations contained in Paragraph 31 of the Complaint.

21. Defendant Holmes admits the allegations contained in Paragraph 32 of the Complaint.

22. Defendant Holmes denies the allegations contained in Paragraph 33 of the Complaint and alleges that defendant Aero Systems sold the assets of Springwater Manufacturing to a subsidiary of defendant Bunnington.

23. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations set forth in Paragraph 34 of the Complaint.

24. Defendant Holmes denies the allegations of Paragraph 35 as applied to defendants Holmes and Aero Systems, and as applied to other defendants, denies knowledge or information sufficient to form a belief concerning the truth of such allegations.

25. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of

the allegations contained in Paragraphs 36 through 55, inclusive of the Complaint.

26. In answer to Paragraph 56 of the Complaint, Defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 55 of this Answer with the same force and effect as if set forth at full length herein.

27. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 57 through 74, inclusive of the Complaint.

28. In answer to Paragraph 75 of the Complaint, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 74 of this Answer with the same force and effect as if set forth at full length herein.

29. Defendant Holmes admits that at certain times he was an officer, controlling person (as defined) and principal shareholder and director of defendant Aero Systems, that at certain times defendant Aero Systems transacted its affairs within the Central District of California on a limited basis, and that defendant Holmes owed a duty to shareholders and purchasers and sellers of the securities of Aero Systems and the investing public to refrain from engaging in unlawful conduct, which duty defendant Holmes alleges was fully satisfied. Defendant Holmes denies knowledge or information sufficient to form a belief whether at "all times relevant" defendant Diamond was an officer, director and controlling person of defendant Bunnington. In all other respects, defendant

Holmes denies the allegations contained in Paragraph 76 of the Complaint.

30. Defendant Holmes admits that on or about July 1976 defendant Aero Systems acquired Springwater Manufacturing and that a wholly owned subsidiary of defendant Bunnington subsequently acquired Springwater Manufacturing. In all other respects, defendant Holmes refers to and hereby incorporates by reference the documents pertaining to such transaction for an accurate description of such transactions. In all other respects, defendant Holmes denies the allegations contained in Paragraph 77 of the Complaint.

31. Defendant Holmes admits the allegations contained in Paragraph 78 of the Complaint.

32. Defendant Holmes admits that for the fiscal year ended February 28, 1979, defendant Aero Systems reported a gain of $442,346 including income tax benefits in connection with the disposition of Springwater Manufacturing. In all other respects, defendant Holmes denies the allegations contained in Paragraph 79 of the Complaint.

33. Defendant Holmes admits the allegations contained in Paragraph 80 of the Complaint.

34. Defendant Holmes denies the allegations contained in Paragraph 81 of the Complaint.

35. Defendant Holmes denies the allegations contained in Paragraph 82 of the Complaint to the extent such allegations apply to defendants Holmes and Aero Systems, and defendant Holmes denies knowledge or information sufficient to form a belief as to the truth of

such allegations to the extent they pertain to other defendants.

36. Defendant Holmes admits that Aero Systems publicly announced during or about April 1980 that it had acquired from Colt Electronics Co., Inc. ("Colt Electronics") a right to exclusively market a computerized fuel management system known as the CD-3000 Fuel Management Computer ("CD-3000"). Defendant Holmes admits that the press releases and shareholder letters identified in subparagraphs (A)-(H) of Paragraph 83 of the Complaint were published, and defendant Holmes refers to and hereby incorporates by reference the complete text of such statements for an accurate description of their contents. Defendant Holmes denies that any of the statements made by defendants Holmes or Aero Systems quoted in Paragraph 83 were misleading or created a misleading impression that sales of the CD-3000 had already been made, and in all other respects defendant Holmes denies the allegations contained in Paragraph 83 of the Complaint.

37. Defendant Holmes denies the allegations contained in Paragraph 84 of the Complaint. Without limiting the generality of the foregoing, defendant Holmes alleges:

(a) the quoted statements did not indicate that any sales of the CD-3000 had been made, and it was not false or misleading to present a reasonable prospect of significant sales in the future at the time at which the statements were made; and

(b) the statements did not vastly overstate, or overstate to any material degree, the potential market for the product; and

(c) the statements never indicated that Aero Systems "would reap a bonanza" as alleged in the Complaint, and such language constitutes itself a false and misleading characterization of the statements made; and

(d) there was a reasonable factual basis for the projected ten percent fuel savings; and

(e) and (f) Aero Systems did not fail to make any disclosure which it was required to make with respect to the terms and conditions of the acquisition of the CD-3000 from Colt Electronics.

38. Defendant Holmes denies the allegations contained in Paragraph 85 of the Complaint and, without limiting the generality of the foregoing, denies that defendant Holmes caused any false or recklessly misleading material misrepresentation to be made regarding Aero Systems sales and projected earnings for fiscal year 1981 and sales and earnings of the CD-3000. Without limiting the generality of the foregoing, defendant Holmes alleges as follows:

(a) the statements made in Moore & Schley, Cameron & Co. Research Department Publication were the responsibility of that entity and not of defendant Holmes;

(b) the statements made in Wheat First Securities Technology Group Publication were the responsibility of that entity and not of defendant Holmes; and

(c) the statements made in an undated Porter, Le Vay & Rose, Inc. Information Report were the responsibility of that entity and not of defendant Holmes;

(d) the statements made in the Alan J. Wax column of the New York Post on October 13, 1980 were the responsibility of that individual and publication and not of defendant Holmes; and

(e) the statements made in the column of Dick Davis in the Miami Herald were the responsibility of that entity and not of defendant Holmes.

39. Defendant Holmes denies the material allegations contained in Paragraph 86 of the Complaint. Without limiting the generality of the foregoing, defendant Holmes alleges as follows:

(a) the interest of potential buyers in the CD-3000 was not misstated, and the prospective market for the CD-3000 at the time was not "very limited";

(b) there were reasonable bases for the projected sales and future earnings to the extent that the projections were made by defendant Holmes, if any; and

(c) there was a reasonable factual basis for the estimated ten percent fuel savings that could purportedly be achieved by users of the CD-3000; and

(d) the statement made that Aero Systems had sold 250 units of the CD-3000 was not made by defendant Holmes.

40. Defendant Holmes denies that the statements made pertaining to completed sales of the CD-3000 were made by or at the direction of defendants Aero Systems

or Holmes, and in all other material respects, defendant Holmes denies the allegations contained in Paragraph 87 of the Complaint.

41. Defendant Holmes admits that the price of Aero Systems stock for 100 shares was quoted in the "pink sheets" by at least one market maker at $2 5/8 bid and $2 3/4 asked during August 1980 and was quoted at a price of $7 bid and $7 1/8 asked in September 1980. In all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 88 of the Complaint.

42. Defendant Holmes denies that the matters alleged, insofar as the same pertain to defendant Holmes, constituted misstatements or misrepresentations or reflected reckless disregard of the truth, and in all other respects, defendant Holmes denies the material allegations contained in Paragraph 89 of the Complaint.

43. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 90 of the Complaint.

44. Defendant Holmes denies the allegations of Paragraph 91 of the Complaint insofar as the same pertain to defendants Holmes and Aero Systems, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of such allegations as the same may apply to other defendants.

45. Defendant Holmes denies the allegations contained in Paragraph 92 of the Complaint.

46. Defendant Holmes admits that at least one securities broker quoted in a "pink sheet" a price of $7 5/8 bid and $7 7/8 asked on May 8, 1981, bid and ask prices of $9 3/8 bid and $ 9 1/2 asked in early December 1980, and $5 1/4 bid and $5 3/8 asked on July 27, 1981 for 100 share lots of shares of Aero Systems. In all other respects, defendant Holmes denies the material allegations contained in Paragraph 93 of the Complaint.

47. Defendant Holmes admits that for the fiscal year ended February 28, 1979, Aero Systems reported net income of $1,300,585. Defendant Holmes also admits that at least one broker quoted a bid for Aero Systems common stock as of February 28, 1979 of approximately $1.90. In all other respects, defendant Holmes denies the material allegations contained in Paragraph 94 of the Complaint.

48. Defendant Holmes admits that Aero Systems reported an income of $0.134 per share for the fiscal year 1980. In all other respects, defendant Holmes denies the material allegations contained in Paragraph 95 of the Complaint.

49. Defendant Holmes denies the material allegations contained in Paragraph 96 of the Complaint.

50. Defendant Holmes denies that he was aware of any fraud and that he sold any shares of Aero Systems with knowledge of any fraud. Without limiting the generality of the foregoing, defendant Holmes denies knowledge or information sufficient to form a belief concerning

the truth of the allegations contained in subparagraphs (A), (B) and (D) of Paragraph 97 of the Complaint. With respect to subparagraph (C) of the Complaint, defendant Holmes admits that defendant Holmes sold approximately 50,000 shares of common stock of Aero Systems at $8.00 per share on or about November 12, 1980 and 25,000 shares of common stock of Aero Systems at $5.00 per share on or about July 24, 1981.

51. Defendant Holmes denies the allegations contained in Paragraph 98 of the Complaint.

52. In answer to Paragraph 99, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 98 of this Answer with the same force and effect as if set forth at full length herein.

53. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 100 through 101, inclusive of the Complaint.

54. Defendant Holmes admits that at certain times he owned securities of Bunnington Corporation. In all other respects, defendant Holmes denies the allegations contained in Paragraph 102 of the Complaint.

55. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 103 and 104, inclusive of the Complaint.

56. Defendant Holmes admits that DCS Financial merged into and with a subsidiary of Aero Systems, that Aero Systems disposed of the assets of Springwater Manufacturing, and in all other respects, defendant Holmes

denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 105 of the Complaint.

57. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 106 of the Complaint.

58. Defendant Holmes expressly denies that any action of defendant Holmes or of defendant Aero Systems facilitated wrongful concealment by any other person or entity and in all other respects, defendant Holmes generally denies the allegations contained in Paragraph 107 of the Complaint.

59. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 108 through 119, inclusive of the Complaint.

60. Defendant Holmes admits that for the fiscal year ended July 31, 1979, Bunnington reported net sales of $9,749,314 and net income of $404,039. In all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 120 of the Complaint.

61. Defendant Holmes admits that for the fiscal year ended July 31, 1980, Bunnington reported a net loss of $708,269. In all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 121 of the Complaint.

62. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 122 through 124, inclusive of the Complaint.

63. Defendant Holmes denies the allegations of Paragraph 125 insofar as the same may pertain to defendants Holmes and Aero Systems, and as to all other defendants, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of such allegations.

64. In answer to Paragraph 126, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 125 of this Answer with the same force and effect as if set forth at full length herein.

65. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 127 through 145, inclusive of the Complaint.

66. In answer to Paragraph 146, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 145 of this Answer with the same force and effect as if set forth at full length herein.

67. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 147 through 171, inclusive of the Complaint.

68. In answer to Paragraph 172, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 171 of this Answer with the same force and effect as if set forth at full length herein.

69. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 173 through 180, inclusive of the Complaint.

70. In answer to Paragraph 181, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 180 of this Answer with the same force and effect as if set forth at full length herein.

71. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 182 through 185, inclusive of the Complaint.

72. In answer to Paragraph 186, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 185 of this Answer with the same force and effect as if set forth at full length herein.

73. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 187 through 189, inclusive of the Complaint.

74. In answer to Paragraph 190, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 189 of this Answer with the same force and effect as if set forth at full length herein.

75. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 191 through 195, inclusive of the Complaint.

76. In answer to Paragraph 196, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 195 of this Answer with the same force and effect as if set forth at full length herein.

77. Defendant Holmes denies any fraudulent manipulation of the price of stock of Aero Systems, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 197 of the Complaint.

78. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 198 of the Complaint.

79. In answer to Paragraph 199, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 198 of this Answer with the same force and effect as if set forth at full length herein.

80. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 200 through 206, inclusive of the Complaint.

81. In answer to Paragraph 207, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 206 of this Answer with the same force and effect as if set forth at full length herein.

82. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 208 through 212, inclusive of the Complaint.

83. In answer to Paragraph 213, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 212 of this Answer with the same force and effect as if set forth at full length herein.

84. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 214 of the Complaint.

85. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 215 through 221, inclusive of the Complaint.

86. In answer to Paragraph 222, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 221 of this Answer with the same force and effect as if set forth at full length herein.

87. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 223 through 231, inclusive of the Complaint.

88. In answer to Paragraph 232, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 231 of this Answer with the same force and effect as if set forth at full length herein.

89. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 233 through 238, inclusive of the Complaint.

90. In answer to Paragraph 239, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 238 of this Answer with the same force and effect as if set forth at full length herein.

91. Defendant Holmes admits that he was aware of the true financial condition of Aero Systems, alleges as a matter of presumption that Aero Systems was aware of the true financial condition of Aero Systems, and in all other respects denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 240 of the Complaint.

92. Defendant Holmes denies that defendants Holmes or Aero Systems knew or recklessly disregarded any information of the type described in Paragraph 241 of the Complaint and alleges that the market price of publicly traded securities is determined by various conditions and events which do not necessarily bear any particular relationship to the reported financial condition of an issuer, as of or at a particular period of time, and in all other respects, defendant Holmes denies the allegations contained in Paragraph 241 of the Complaint.

93. Defendant Holmes denies that defendant Holmes, or to his knowledge, defendant Aero Systems, provided any of the assistance described in Paragraph 242 of the Complaint, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 242 of the Complaint.

94. Defendant Holmes denies the allegations contained in Paragraphs 243 through 245, inclusive of the Complaint as the same pertain to defendants Holmes and

Aero Systems, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of such allegations.

95. In answer to Paragraph 246, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 245 of this Answer with the same force and effect as if set forth at full length herein.

96. Defendant Holmes denies the allegations contained in Paragraphs 247 and 248, inclusive of the Complaint as the same pertain to defendants Holmes and Aero Systems and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of such allegations.

97. Defendant Holmes denies the existence of an alleged "Aero Systems manipulation" as purportedly described in the Second Claim for Relief and incorporates by reference the Answer of defendant Holmes to each allegation of the Second Claim For Relief, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 249 of the Complaint.

98. Defendant Holmes denies the allegations contained in Paragraphs 250 through 254, inclusive of the Complaint as the same pertain to defendants Holmes and Aero Systems, and as to all other defendants, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of such allegations.

99. Defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 254 of this

Answer with the same force and effect as if set forth at full length herein.

100. Defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraphs 256 through 258, inclusive of the Complaint.

101. In answer to Paragraph 259, defendant Holmes repeats and realleges the allegations contained in Paragraphs 1 through 258 of this Answer with the same force and effect as if set forth at full length herein.

102. Defendant Holmes denies that defendants Holmes or Aero Systems were aware of any false representations of the nature described in Paragraph 260 of the Complaint, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 260 of the Complaint.

103. Defendant Holmes denies making any false representations as alleged in Paragraph 261 of the Complaint, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of allegations contained in Paragraph 261 of the Complaint.

104. Defendant Holmes denies the allegations contained in Paragraph 262 of the Complaint as the same pertain to defendants Holmes and Aero Systems, and in all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of such allegations.

105. Defendant Holmes denies the allegations contained in Paragraph 263 of the Complaint to the extent the same may apply to defendants Holmes and Aero Systems. In all other respects, defendant Holmes denies knowledge or information sufficient to form a belief concerning the truth of the allegations contained in Paragraph 263 of the Complaint.

FIRST AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Failure to State a Claim)

106. The Complaint fails to state any claim upon which relief can be granted.

SECOND AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Statute of Limitations)

107. The Complaint and purported claims for relief are barred in whole or in part by California Code of Civil Procedure Section 338(4).

108. The Complaint and purported claims for relief are barred in whole or in part by California Code of Civil Procedure Section 343.

109. The Complaint and purported claims for relief are barred in whole or in part by California Corporations Code Section 25506.

THIRD AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Laches)

110. Plaintiffs knew, or in the exercise of reasonable care should have known of the events and conditions of which they complain, if any existed (and without admitting that any existed), at a time not presently known to defendant Holmes but known to plaintiffs, and in all events prior to the respective collapses of Sebag and FSSC. Notwithstanding such knowledge, plaintiffs failed to take any action to avoid or reduce the injuries now alleged, including, without limitation, any action by way of resort to judicial remedies, prior to instituting this action. Plaintiffs are barred, therefore, in whole or in part by the doctrine of laches from recovery.

FOURTH AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Estoppel)

111. Plaintiff trustees or their predecessors in interest knew of the misrepresentations, omissions and manipulative scheme alleged in their Complaint, if any existed (and without admitting that any existed), but continued to make markets in the securities affected thereby. Defendant Holmes reasonably and in good faith relied upon the market price of the securities as well as upon the other acts and statements of plaintiffs or their predecessors in interest, in making any statements and undertaking any acts alleged in plaintiffs' Complaint. Plaintiffs are estopped, therefore, in whole or in part from recovery.

FIFTH AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Failure to Avoid or Mitigate Damages)

112. After the respective collapses of Sebag and FSSC, plaintiffs failed to take any or all actions reasonable or necessary under the circumstances to avoid or reduce the injuries alleged. Plaintiffs are therefore barred in whole or in part by their failure to avoid or mitigate damages from recovery.

SIXTH AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Plaintiffs at Fault)

113. Plaintiffs or their predecessors in interest are at fault in causing the injuries alleged and are barred, therefore, in whole or in part from recovery.

114. Plaintiffs, by virtue of their or their respective predecessors' knowledge of and participation in the alleged misrepresentations, omissions and manipulative scheme, if any, are barred in whole or in part by the doctrine of unclean hands from recovery.

SEVENTH AFFIRMATIVE DEFENSE TO ALL CLAIMS FOR RELIEF

(Unreasonable Reliance)

115. Plaintiffs did not rely on alleged misrepresentations or omissions, if any, by defendant Holmes. Any reliance by plaintiffs was, in any event, unreasonable under all of the circumstances. Plaintiffs are barred, therefore, in whole or in part from recovery.

116. Plaintiffs or their predecessors in interest, through the exercise of reasonable diligence, could have discovered all of the facts allegedly misrepresented or concealed by defendant Holmes. Plaintiffs unreasonably and recklessly failed to conduct any and all investigations reasonable or necessary under the circumstances into such facts, notwithstanding that they were professional dealers and otherwise sophisticated investors in securities and who knew or should have known facts sufficient to put them on notice of a need to inquire further as to such facts. Plaintiffs are barred, therefore, in whole or in part from recovery.

EIGHTH AFFIRMATIVE DEFENSE TO
ALL CLAIMS FOR RELIEF

(Collateral Estoppel)

117. The Complaint and claims for relief, to the extent that they raise and rely upon issues of fact that were determined in *SEC v. Newport Securities Corp.*, are barred in whole or in part by the doctrine of collateral estoppel.

NINTH AFFIRMATIVE DEFENSE TO
ALL CLAIMS FOR RELIEF

(Lack of Standing)

118. At no time were plaintiffs either purchasers or sellers of the securities of Aero Systems. Plaintiffs therefore lack standing under Section 10 or Rule 10b-5 of the Exchange Act to recover on the Complaint.

119. Plaintiff SIPC's recovery is limited to such claims as it may acquire by right of subrogation through payments actually made to customers of Sebag and FSSC, respectively, on the net equity claims of such customers. SIPC is therefore barred from recovery on the Complaint of any sums in excess of such payments to customers, including, without limitation, any claims for treble or punitive damages.

120. Plaintiff SIPC insured only the value of securities of customers left on deposit with Sebag and FSSC as of the dates of the filings of their respective liquidations. The net equity claims asserted by SIPC based upon such values were not the proximate result of any of defendant Holmes' alleged acts. Plaintiff SIPC is barred, therefore, in whole or in part from recovering against Holmes on the Complaint.

121. Plaintiff trustees' recovery is limited by law to such claims as might have been asserted against defendant by Sebag or First State themselves. Plaintiff trustees lack standing to assert claims on behalf of customers of Sebag or FSSC. Plaintiff trustees are barred, therefore, in whole or in part from recovery on the Complaint.

122. Sebag and FSSC, through their agents, employees, officers, directors and shareholders, were knowing participants in the manipulative scheme and misrepresentations and omissions alleged. Plaintiff trustees are barred, therefore, in whole or in part from recovery.

TENTH AFFIRMATIVE DEFENSE TO
ALL CLAIMS FOR RELIEF

(Good Faith and Due Diligence)

123. Defendant Holmes duly and diligently performed all investigations of the facts underlying the statements or omissions alleged to have been made or omitted to have been made by him. Any statements by defendant Holmes were made in good faith and without knowledge of any falsity thereof or of any need to disclose any fact not disclosed. Defendant Holmes honestly believed in the truth and completeness of all statements allegedly made by him, and could not in the exercise of reasonable diligence have discovered the falsity or incompleteness thereof, if any. Plaintiffs are barred, therefore, in whole or in part from recovery.

ELEVENTH AFFIRMATIVE DEFENSE TO
ALL CLAIMS FOR RELIEF

(Set Off)

124. To the extent that any of plaintiffs' claims against any other persons arising out of the same transactions or occurrences alleged in plaintiffs' Complaint have been or are compromised prior to judgment herein, defendant Holmes is entitled to set off the entire amount of such compromised claims against his alleged liability to plaintiffs.

FIRST AFFIRMATIVE DEFENSE TO PLAINTIFFS'
SEVENTEENTH (RICO) CLAIM FOR RELIEF

(No Criminal Proceeding)

125. Defendant Holmes is not guilty of, and has not been adjudged guilty of nor indicted for or charged with,

any of the criminal acts alleged in the Complaint. Plaintiffs are barred, therefore, in whole or in part from recovering on the Seventeenth Claim for Relief.

SECOND AFFIRMATIVE DEFENSE TO PLAINTIFFS'
SEVENTEENTH (RICO) CLAIM FOR RELIEF

(Statute of Limitations)

126. The Seventeenth Claim for Relief is barred in whole or in part by Section 338(1) of the California Code of Civil Procedure.

127. The Seventeenth Claim for Relief is barred in whole or in part by Section 340(1) of the California Code of Civil Procedure.

128. The Seventeenth Claim for Relief is barred in whole or in part by Section 343 of the California Code of Civil Procedure.

THIRD AFFIRMATIVE DEFENSE TO PLAINTIFFS'
SEVENTEENTH (RICO) CLAIM FOR RELIEF

(No Relationship to Organized Crime)

129. The enterprise alleged in the Complaint had no involvement or relationship with any person engaged in organized crime or with any organized crime activities. Plaintiffs are barred, therefore, in whole or in part from recovery.

FOURTH AFFIRMATIVE DEFENSE TO
PLAINTIFFS' SEVENTEENTH (RICO)
CLAIM FOR RELIEF

(Alternative Remedies)

130. Plaintiffs have adequate remedies under the federal securities laws, including Section 10 and Rule

10b-5 of the Exchange Act for all injuries allegedly caused by defendant Holmes, and are barred, therefore, in whole or in part from recovering on their Seventeenth Claim for Relief.

FIFTH AFFIRMATIVE DEFENSE TO PLAINTIFFS' SEVENTEENTH (RICO) CLAIM FOR RELIEF

(No RICO Injury)

131. Plaintiffs have not been injured by reason of a violation of 18 U.S.C. Section 1962, and are barred, therefore, in whole or in part from recovery on the Seventeenth Claim for Relief.

132. Plaintiffs have not suffered any competitive injury as a result of any acts of defendant Holmes alleged in the Complaint, and are barred, therefore, in whole or in part from recovery on the Seventeenth Claim for Relief.

SIXTH AFFIRMATIVE DEFENSE TO PLAINTIFFS' SEVENTEENTH (RICO) CLAIM FOR RELIEF

(No Vicarious Liability)

133. Defendant Holmes cannot be held vicariously liable under 18 U.S.C. Section 1962 or 18 U.S.C. Section 1964 for the acts of any other person or entity alleged in the Complaint. Plaintiffs are barred, therefore, in whole or in part from recovery on the Seventeenth Claim for Relief.

SEVENTH AFFIRMATIVE DEFENSE TO PLAINTIFFS' SEVENTEENTH (RICO) CLAIM FOR RELIEF

(Denial of Due Process)

134. Because 18 U.S.C. Section 1962 seeks to deprive defendant Holmes of liberty or property without due process of law, in that it purports to render defendant Holmes answerable for the acts of other persons whose acts and whose relationship to defendant Holmes through an alleged "enterprise" or "pattern" or activity are fortuitous, unknown, and not reasonably knowable or reasonably foreseeable by defendant Holmes, plaintiffs' claim based upon that section is barred by the Fifth Amendment to the United States Constitution.

Dated: April 3, 1985

Respectfully submitted,
JACK I. SAMET
BUCHALTER, NEMER, FIELDS, CHRYSTIE & YOUNGER

/s/ Jack I. Samet
Jack I. Samet
Attorneys for Defendant
ROBERT G. HOLMES, JR.

VERIFICATION

STATE OF CALIFORNIA, COUNTY OF

I have read the foregoing _____

_____ and know its contents.

X CHECK APPLICABLE PARAGRAPH

___ I am a party to this action. The matters stated in it are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

___ I am ___ an Officer ___ a partner ___ a ___ of ___

_____

a party to this action, and am authorized to make this verification for and on its behalf, and I make this verification for that reason. I have read the foregoing document and know its contents. The matters stated in it are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

___ I am, one of the attorneys for _____ a party to this action. Such party is absent from the county of aforesaid where such attorneys have their offices, and I make this verification for and on behalf of that party for that reason. I have read the foregoing document and know its contents. I am informed and believe and on that ground allege that the matters stated in it are true.

Executed on _____ 19___, at _____ California.

_____

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

_____

Signature

ACKNOWLEDGEMENT OF RECEIPT OF DOCUMENT
(other than summons and complaint)

Received copy of document described as _____

_____

on _____ 19___.

_____

Signature

PROOF OF SERVICE BY MAIL

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 700 South Flower Street, Los Angeles, California 90017-4183.

On Apr. 3, 1985, I served the foregoing document described as Answer of Defendant Robert G. Holmes, Jr. to First Amended Complaint for Damages on the parties having appeared in this action by placing a true copy thereof enclosed in a sealed envelope with postage thereon fully prepaid in the United States mail at: Los Angeles, California 90017. addressed as follows:

PLEASE SEE ATTACHED LIST FOR NAMES OF PARTIES SERVED

XX (BY MAIL) I caused such envelope with postage thereon fully prepaid to be placed in the United States mail at Los Angeles, California.

___ (BY PERSONAL SERVICE) I caused such envelope to be delivered by hand to the offices of the addressee. Executed on April 3, 1985 at Los Angeles, California.

___ (State) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

X (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

STUARTS EXBROOK; TIMESAVER (REVISED 7/81)
(May be used in California State or Federal Courts)

Signature
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IN SIPC v. VIGMAN, et al.
(Pleadings)

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR PROTECTION CORPORATION, et al., Plaintiffs, vs. SEYMOUR VIGMAN, et al., Defendants. AND CONSOLIDATED ACTIONS.	CASE NO. CV 83-4742-AWT (Tx) [Consolidated Cases] DEFENDANT ROBERT G. HOLMES, JR.'S STATEMENT OF UNCONTROVERTED FACTS AND CONCLUSIONS OF LAW IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT WITH RESPECT TO CLAIMS ASSERTED UNDER THE RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS ACT (RICO) (AMENDED) DATE: October 17, 1988 TIME: 10:00 a.m. PLACE: Courtroom of the Honorable A. Wallace Tashima

Defendant Robert G. Holmes, Jr. ("Holmes") respectfully submits the following Amended Statement of Uncontroverted Facts and Conclusions of Law to supercede his previously filed Statement of Uncontroverted Facts and Conclusions of Law filed pursuant to Local Rule 7.14.1 of the above-entitled Court in support of his Motion For Summary Judgment With Respect To Claims Asserted Under The Racketeer Influenced And Corrupt Organizations Act (RICO) (the "RICO Motion").

UNCONTROVERTED FACTS

1. Neither Holmes nor Aero Systems was involved in any significant business or personal transaction with any of the following entities or with any officer or employee of any of these entities:

> Creditbank, Inc. (Exhibit 1, Calonge Depo. 4-29-87, p. 9:19-10:5)
>
> (all deposition testimony herein cited is contained in a set of Exhibits filed concurrently herewith).

Ibebafin, S.A. (no evidence of any connection with Holmes or Aero Systems)

Keops, S.A. (no evidence of any connection with Holmes or Aero Systems)

Talingo Corporation (no evidence of any connection with Holmes or Aero Systems)

Tula Corporation (no evidence of any connection with Holmes or Aero Systems)

2. Holmes was not involved in any significant transactions nor had any significant business or personal communications with any of the following individual "RICO

Defendants": Rodger Garrity, (Exhibit 9, Holmes Depo. of 12-4-87, p. 269:6-270:9) Frankie Mae Garrity; (no evidence of connection with Holmes): Herbert Frank (Exhibit 6, Frank Depo. of 12-8-87 and 12-9-87, p. 137:14-138:8; Exhibit 7, Holmes Depo. of 12-3-87, p. 156:24-157:6), Velma Shaw (no evidence of any connection with Holmes), Jose Luis Calonge (Exhibit 1, Calonge Depo. of 4-29-87, p. 9:19-23), Delores Owens Cipparrone, (Exhibit 10, Holmes Depo. of 2-23-88, p. 1197:17-1198:2); Jay Dash (Exhibit 2, Dash Depo. of 7-28-87, p. 60:20-22), Phillip Dash (Exhibit 11, Holmes Depo. of 2-24-88, p. 1327:22-1328:2), Elliott Eiseman (Exhibit 4, Eiseman Depo. of 5-7-86, p. 215:12-19), David Goldman (no evidence of connection found), Jack Haber (Exhibit 8, Haber Depo. of 7-6-86, p. 59:16-65:15), Jose Camprubi Sala (no evidence of connection on [sic] found).

3. Aero Systems had limited business transactions involving Aerosonic, the sale of altimeters and other avionics products to Aero Systems over the last 20 years. (Holmes Depo. of 12-3-87, p. 155:17-156:17).

4. In approximately 1970, Aerosonic merged with an entity called Instrument Technologies which was a subsidiary of Aerotech. Aerotech was at one time a subsidiary of Aero Systems, other than this remote connection to Aero Systems, and its limited sales of avionics products to Aero Systems, Aerosonic had no other significant business or other relationship with Holmes or Aero Systems. (Exhibit 6, Frank Depo. of 12-8-87 and 12-9-87, p. 120:14-19, p. 122:15-22).

5. Herbert Frank, who was President of Aerosonic, had no personal knowledge of, or relationship with,

Holmes. (Exhibit 6, Frank Depo. of 12-8-87 and 12-9-87, p. 137:14-138:8; Exhibit 7, Holmes Depo. of 12-3-87, p. 156:24-157:3).

6. Holmes had no position of authority, and exercised no control, over any of the following entities:

> Executive Securities (Exhibit 3, Eiseman Depo. of 11-22-85, p. 42:17-43:5, p. 50:17-52:13, p. 53:9-54:11)
>
> Newport Securities (Exhibit 16, Susson Depo. of 2-22-88, p. 22:3-33:24)
>
> First State Securities Corporation ("FSSC") (Exhibit 3, Eiseman Depo. of 11-22-85, p. 63:13-23)
>
> Joseph Sebag, Inc. ("Sebag") (Exhibit 15, Myers SEC Testimony, 9-1-85, p. 11:17-13:7, p. 30:4-18, p. 36:1-39:6)

7. Between 1976 and 1981, FSSC and Sebag traded Aero Systems securities on the over-the-counter market ("OTC") and Holmes had an account at FSSC but neither Holmes nor Aero Systems had any other transactions with FSSC and Sebag whichever not related to the trading of Aero Systems securities. Holmes did not direct or control the trading of OTC stocks, including Aero Systems stock, at FSSC or at Sebag. (*See* No. 3 above).

8. Holmes' only interest at FSSC was as a customer. Holmes had no interest in and was not a customer at Sebag. (Exhibit 5, Foley Depo. of 6-22-88, p. 265:23-266:14).

9. Holmes has never been employed by J.C. Roberts, or Executive Securities, or by Newport Securities, or by either FSSC or Sebag. (*See* No. 3 above.)

10. Holmes was introduced to Seymour Vigman ("Vigman") in 1966 by Murray Silvershein. Silvershein was a friend of Ralph Gordon, who was Aero Systems' accountant at the time. (Exhibit 11, Holmes Depo. of 2-23-88, p. 1132:19-23 and Exhibit 12, Holmes Depo. of 2-25-88, p. 1371:5-22).

11. At the time Holmes met Vigman, Vigman was a registered broker at J.C. Roberts and had been in the securities brokerage business since at least 1962.

12. At the time Holmes met Vigman, Holmes was interested in a public offering of Aero Systems stock, in part, to make a market for Aero Systems stock in which Holmes' family could easily sell their Aero Systems stock to generate income. Holmes did not believe that his family could effectively operate Aero Systems to generate income for their support. (Exhibit 11, Holmes Depo. of 2-23-88, p. 1155:11-1156:25).

13. In 1966 Vigman, through J.C. Roberts, agreed to underwrite the public offering of Aero Systems' securities of up to 100,000 shares, based upon Aero Systems' financial statements presented to him by Holmes and Gordon. (Exhibit 11, Holmes Depo. of 2-23-88, p. 1155:11-1156:18).

14. Aero Systems' 1967 public offering was accomplished through J.C. Roberts which commenced to make a market in Aero Systems' securities in 1967, around 30 days after the offering. (Exhibit 17, Vigman Depo. of 5-5-88, p. 713:15-19).

15. Joseph Lugo ("Lugo") was an employee at J.C. Roberts in 1964 until 1967 but worked only in the back office and not as a broker. Holmes had no significant

contact with Lugo while Lugo was at J.C. Roberts. (Exhibit 14, Lugo Depo. of 11-9-87, p. 36:7-14 and Exhibit 11, Holmes Depo. of 2-23-88, p. 1146:3-16).

16. Holmes was not a party to the SEC's consent decree against Vigman in 1967 which led to the winding up of J.C. Roberts. The conduct alleged by the SEC to be unlawful and which led to the consent decree against Vigman in 1967 did not involve Holmes. The SEC's allegations in such respect did not implicate Holmes in Vigman's alleged wrongdoing. (See Exhibit "19").

17. Holmes was not involved in any decision by Vigman to purchase or resell any Aero Systems' warrants issued through J.C. Roberts that were allegedly not also offered to the public in or around 1967. (Exhibit 11, Holmes Depo. of 2-23-88, p. 1166:12-25).

18. The price of Aero Systems' securities traded by Executive Securities, Newport Securities and Garrity was the true and intrinsic price of that stock.

19. Holmes never participated in the management of, or making of decisions at, either Executive Securities or Newport Securities. (Exhibit 3, Eiseman Depo. of 11-22-85, pp. 42:17-43:5, p. 50:17-52:13, p. 53:9-54:11 and Exhibit 16, Susson. 2-22-88, p. 22:3-33:24; Exhibit 7, Holmes Depo. of 12-3-87, p. 146:12-147:6).

20. There were no mechanisms in place at either Executive Securities or Newport Securities for controlling or directing Holmes' or Aero Systems' affairs and in fact no such control or direction ever occurred. (*See* par. 19 above).

21. The only management "position" or "role" which Holmes held in any organization amongst the identified defendants was in Aero Systems. (*See* par. 6 above).

22. Aero Systems was the only entity in which Holmes had operational involvement or control. (*See* par. 6 above).

23. Holmes had no ownership interest in, nor controlled or directed the affairs of, Creditbank. (Exhibit 1, Calonge Depo. of 4-29-87, p. 9:19-10:5).

24. Holmes' sole interest in Bunnington was as a shareholder.

25. Holmes held no management position in Bunnington and did not control or direct the affairs of Bunnington. (Exhibit 13, Holmes Depo. of 5-5-88, p. 2576:2-16).

26. When Aero Systems issued warrants as part of its public offering in 1967, this was a capital-raising endeavor also intended by Holmes to create a public market for Aero Systems securities. (Exhibt [sic] 11, Holmes Depo. of 2-23-88, p. 1157:9-13).

27. Holmes did not make any false representations to any person in connection with the issuance of Aero Systems warrants in 1967. (Exhibit 11, Holmes Depo. or [sic] 2-23-88, p. 1166:12-24).

28. Holmes did not make any false representations to any person in connection with the merger of DCS Financial and Aero Systems in 1976. (*See* Exhibit "18").

29. Aero Systems merger with DCS Financial in 1976 was, in part, motivated by Aero Systems' desire to regain the contract rights to the DC 10 aircraft parts which DCS Financial had obtained from Aero Systems by providing the cash Aero Systems needed for the down-payment to Frederick D. Ayer ("Ayer"). (Exhibit 12, Holmes Depo. of 2-24-88, p. 1283:25-1285:20; Exhibit 13, Holmes Depo. of 2-25-88, p. 1440:17-1441:6).

30. In 1976, at or about the time of the DCS Financial merger transaction, Holmes, and the management at Aero' Systems, did not think it convenient for Aero Systems to use its operating funds for the cash down-payment to Ayer for the contract rights to the crashed DC 10 airline parts. (Exhibit 12, Holmes Depo. of 2-24-88, p. 1287:5-11).

31. In or around November 1975, Holmes discussed the purchase of the DC 10 airline parts with Vigman, a controlling shareholder in DCS Financial. (Exhibit 12, Holmes Depo. of 2-24-88, p. 1335:14-1336:20).

32. Isadore Diamond, who was a shareholder in DCS Financial, proposed that DCS Financial purchase one-half of Aero Systems' rights to the airline parts for $50,000 and advance to Aero Systems $100,000 for the deposit to be made to Ayer. (Exhibit 12, Holmes Depo. of 2-24-88, p. 1336:2-1337:5).

33. The DCS Financial merger was accomplished in mid July 1976. (Exhibit 12, Holmes Depo. of 2-24-88, p. 1396:12-1397:8).

34. The DCS Financial merger with a subsidiary of Aero Systems enabled Aero Systems to obtain $250,000 in

cash which DCS Financial had on hand. (Exhibit 13, Holmes Depo. of 2-25-88, p. 1440:17-24).

35. The DCS Financiai merger enabled Aero Systems to reclaim one-half of the Ayer DC 10 parts contract rights which Aero Systems had initially transferred to DCS Financial in partial consideration of the cash deposit advance from DCS Financial. (Exhibit 13, Holmes Depo. of 2-25-88, p. 1440:17-1441:12).

36. Springwater Manufacturing was a profitable subsidiary of DCS Financial which Aero Systems acquired as part of the merger transaction. (Complaint, par. 78) (Exhibit 13, Holmes Depo. of 2-25-88, p. 1440:17-1441:6).

37. The DCS Financial merger transaction with Aero Systems enabled Aero Systems to claim DCS Financial's tax loss carry-forward to the benefit of Aero Systems in accordance with applicable tax laws. (Exhibit 13, Holmes Depo. of 2-25-88, p. 1440:17-1441:12).

38. As part of the DCS Financial merger transaction, Springwater Manufacturing was required to maintain its net worth as a condition to Aero Systems' transferring to the DCS Financial shareholders certain Aero Systems' shares which were held in escrow. (Exhibit 13, Holmes Depo. of 2-25-88, p. 1493:22-24, p. 1494:18-20, p. 1495:1-5).

39. As part of the DCS Financial merger transaction, Springwater Manufacturing had to repay to Aero Systems at least $200,000 of Aero Systems' then outstanding debt to DCS Financial. (Exhibit 13, Holmes Depo. of 2-25-88, p. 1495:6-20).

40. As part of the DCS Financial merger transaction, Springwater Manufacturing was required to obtain long term financing. (Exhibit 13, Holmes Depo. of 2-25-88, p. 1495:21-1496:24).

CONCLUSIONS OF LAW

1. There is no identifiable "racketeering enterprise" that is separate and distinct from the alleged pattern of racketeering activity.

2. There is no identifiable "racketeering enterprise" that is an ongoing organization in fact of ascertainable structure amongst the "RICO Defendants."

3. Holmes did not invest any income derived from a pattern of racketeering activity in any enterprise engaged in interstate commerce.

4. Holmes did not acquire, through a pattern of racketeering activity, an interest in or control of an enterprise.

5. Holmes was not employed or associated with an enterprise and did not conduct the affairs of any enterprise through a pattern of racketeering activity.

6. Holmes did not conspire to violate Sections 1962(a); 1962(b); 1962(c) of RICO 18 U.S.C. 1961 *et seg.*

7. The alleged predicate acts are not offenses involving fraud in the sale of securities or bankruptcy fraud under Title 11, U.S.C., or acts indictable as mail or wire fraud under Title 18, U.S.C. §§ 1341, 1343.

8. The alleged "predicate acts" are not racketeering activity as defined in RICO Section 1961(1).

9. There are not at least two "predicate acts" occurring within ten years of each other which are sufficiently related or continuous to constitute a "pattern" of racketeering activity.

10. The "predicate acts" alleged did not cause the injuries of the Securities Investor Protection Corporation ("SIPC") and/or the injuries of the Trustees appointed by SIPC to liquidate Joseph Sebag, Inc. ("Sebag") and First State Securities Corporation ("FSSC").

11. SIPC does not meet the "purchaser-seller" requirements for standing to assert RICO claims which are predicated upon violation of Section 10(b) and Rule 10b-5 of the 1934 federal Securities Exchange Act.

DATED: August 15, 1988

Respectfully submitted,

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BUCHALTER, NEMER,
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A Professional Corporation

By /s/ Stephen K. Lubega
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STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 700 South Flower Street, Suite 700, Los Angeles, California 90017.

ON August 15, 1988, I served the foregoing document described as DEFENDANT ROBERT G. HOLMES, JR.'S STATEMENT OF UNCONTROVERTED FACTS IN SUPPORT OF HOLMES' MOTION FOR SUMMARY JUDGMENT WITH RESPECT TO CLAIMS ASSERTED UNDER THE RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS ACT (RICO) on all interested parties in this action

[X] by placing the true copies thereof enclosed in sealed envelopes addressed as stated on the attached mailing list:

[ ] by placing [] the original [] a true copy thereof enclosed in sealed envelopes addressed as follows:

[X] BY MAIL

[ ] *I deposited such envelope in the mail at Los Angeles, California. The envelope was mailed with postage thereon fully prepaid.

[X] I caused such envelope to be deposited in the mail at Los Angeles, California. The envelope was mailed with postage thereon fully prepaid.

I am "readily familiar" with firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. postal service on that same day in the ordinary course of business. I am aware that on motion of

party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date of deposit for mailing in affidavit.

Executed on August 15, 1988, at Los Angeles, California.

[ ] **(BY PERSONAL SERVICE) I delivered such envelope by hand to the offices of the addressee. Executed on, 1988, at Los Angeles, California.

[ ] (State) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Jean Simmons	/s/ Jean Simmons
Name	Signature

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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR PROTECTION CORPORATION, et al., Plaintiffs, v. SEYMOUR VIGMAN, et al., Defendants. AND CONSOLIDATED ACTIONS.	Case No. CV 83-4742-AWT (Tx) (Consolidated Cases) STATEMENT OF BACKGROUND AND FACTS [Filed Concurrently with Memoranda of Points and Authorities in Opposition to Holmes' Motions for Summary Judgment] [Filed Concurrently with Plaintiffs' Statement of Genuine Issues] DATE: October 17, 1988 TIME: 10:00 a.m. PLACE: Courtroom of Honorable A. Wallace Tashima

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I

INTRODUCTION

The entire thrust of Defendant Robert G. Holmes, Jr.'s ("Holmes") Motion for Summary Judgment is that the conduct of Defendant Joseph A. Lugo, Jr. ("Lugo") and other defendants were independent forces for which Holmes cannot be accountable. The facts, as hereinafter set forth, show that Holmes is not only culpable, but along with defendants Seymour Vigman ("Vigman") Isadore Diamond ("Diamond"), Martin Blumenthal ("Blumenthal"), Lugo and Rodger Garrity ("Garrity"), was one of the principal characters in the scheme to manipulate Aero Systems, Inc. ("Aero Systems") and prices of other over-the-counter securities.

Lugo did not act alone. Rather, the scheme, as will be shown, required and had participants each with distinct roles and responsibilities, with each profiting in his own way, and each contributing to the collapse of First State Securities Corporation (*"FSSC"*) and Joseph Sebag Incorporated (*"Sebag"*).

II

STATEMENT OF BACKGROUND AND FACTS

A. HOLMES IS LIABLE FOR DAMAGE CAUSED BY THE MANIPULATIVE SCHEME

As more fully set forth below, Holmes was a longtime friend and confident of Lugo and Vigman. His relationship with Lugo and Vigman enabled him to successfully manipulate Aero Systems and Bunnington stocks. More importantly, however, the Aero Systems manipulation

was only a component of a larger scheme to manipulate six different securities. The manipulative schemes culminated with the demise of FSSC and Sebag, thus causing harm to the Trustees and SIPC.

The manipulated securities were Aerosonic, Aero Systems, Bunnington, Creditbank, Dash and Osrow. Holmes' involvement with the grand scheme included the following acts: (1) the manipulation of Aero Systems' stock which benefited Vigman, who sold out large positions at the precise moment that false press releases caused the price to escalate. Lugo then resold the Aero Systems stock which harmed FSSC, when Lugo used profits from Aero Systems sales to increase FSSC's inventory position in Bunnington and Aerosonic stock, in a further attempt to manipulate those stocks for the benefit of Holmes, among others; (2) the utilization of proceeds from the sale of Aero Systems stock at manipulated prices to purchase Bunnington stock, when Vigman failed to demand immediate payment. This created a false cash supply at FSSC, enabling Lugo to buy up Bunnington and Aerosonic stock, thereby creating the appearance of market activity when, in fact, there was no *bona fide* market activity in Bunnington or Aerosonic stock; (3) the direct participation in a manipulation of Bunnington stock through the dissemination of a false and misleading press release to a stock broker; (4) the direct manipulation of Bunnington stock through a pattern of trading consisting of purchasing Bunnington stock at FSSC in relatively large blocks, and selling the stock at other brokerage houses in small increments to create the appearance of a wellspread market that did not exist; (5) the parking of 5,000 shares of Bunnington stock at a crucial time when

Lugo needed to get Bunnington stock off FSSC's books thereby enabling FSSC to stay in business past the point of a net capital deficiency; (6) the agreement of Holmes to allow his company, Aero Systems, to serve as a retail outlet for a computer marketed by Dash Industries, thereby enabling Dash Industries to make false and misleading statements regarding its business and prospects.

Plaintiffs submit that Holmes was a knowing participant in the manipulative scheme to inflate the price of all six securities. Holmes' knowledge of the scheme's scope and complexity is not only evident in the acts identified above, but can also be inferred from his long-standing relationships with other players in the scheme, and the personal benefit he realized from marketing securities. Those relationships with his co-defendants are described below.

Plaintiffs seek to prove that the course of Holmes' conduct, stretching back to the mid 1960's, shows a method of operation that became highly sophisticated by 1980-1981. Further, the relationships of many years and acts of many years ago indicate the formation of a conspiracy to manipulate securities that continues to this day. Moreover, many of the activities outlined below are predicate acts under the Racketeer Influenced and Corrupt Organizations Act.

B. HOLMES AND AERO SYSTEMS, INC.

Aero Systems has been described as " . . . a company specializing in buying, reconditioning and recertifying, through the Federal Aviation Administration, used instruments and parts from junked airplanes, and then

selling them as replacement parts" (Exh. 2621, p. 9). The industry refers to operations like Aero Systems as "junk dealers" (Hayden, pp. 58-59).

1. Holmes' Control Over Aero Systems.

Holmes strictly controlled the activities of Aero Systems. He was President, Chairman of The Board of Directors and Chief Executive Officer. (Jackson, p. 6; Aero Systems Annual Reports 1975-1982, Exhs. 5253-5261).

Holmes admits that he has been Chairman of the Board of Directors and President of Aero Systems since 1962. (Holmes Response to Requests for Admissions ["RFA"] 112-115). At the time Aero Systems "went public" in 1967, the preliminary prospectus described Holmes as "founder, executive officer and director of the company since it business inception in 1951" (Exh. 5290). Between 1976 and 1981, Holmes and his wife held between 38% and 20% of the issued and outstanding stock in Aero Systems (Exhs. 5262, 5263, 5264, 5266, 5267 and 5268). Holmes did not hold regular Board Meetings (Jackson, pp. 8-9; Holmes, p. 2374). Holmes was involved in nearly every aspect of the company, and had full control over everything that was going on (Jackson, pp. 7-8; 30; 48; 54).

In addition to his strict oversight of all of the affairs of Aero Systems, Holmes always held a controlling block of Aero Systems common stock. Holmes was a controlling person within the meaning of the Federal securities laws as of October 13, 1978 (RFA 803).

2. Holmes' philosophy regarding "values" underlying Aero Systems stock price.

Since Aero Systems became a corporation in March 1967, Holmes developed and cultivated a relationship with Aero Systems' market makers which Holmes calls "Sponsorship." (Holmes, Exh. 3955). Holmes believes that "Sponsorship" is "the real secret to the future success of any public company" (*Id.*). Without it, "[t]here is no one to create new market interest in the Company. Without new interest the stock price deteriorates . . . " (*Id.*). Holmes did not believe that the controlling factors concerning a stock's price on the open market are traditional measures such as net worth or earnings or book value or sales of the company (Holmes, p. 2643). Rather, Holmes believed, that by simply maintaining a particular kind of relationship with his market makers, he could maintain a high public value of Aero Systems shares with little or no economic basis compared to those companies which had high earnings per share, low price to earnings ratios, dividends, high sales and high net worth (Holmes, Exh. 3954).

Rather than recognize the traditional basis for the value of a stock, it is significant to the pattern of facts in this case that Holmes believes that the key ingredient to the value of a company's stock is " . . . the way that it [the company] presents itself and the way that the company *appears* to the brokers who may be interested in the stock, what they believe or perceive to be the future potential for that company" (Holmes, p. 2644) (emphasis added).

Holmes acknowledges that the CD-3000 (a "fuel management" device which was the subject of numerous false public statements,) is a key example of a device used by

Holmes to influence "Sponsors" who might "believe or perceive [it] to be the future potential" for Aero Systems (Holmes, p. 2644). Indeed, it is exactly this philosophy, belief and practice, united with what his "Sponsors" might believe or perceive, which underlines Holmes' deception of the public after Aero Systems acquired the "world-wide distribution rights" to the CD-3000 on March 27, 1980.

C. ROBERT HOLMES AND SEYMOUR VIGMAN.

1. Vigman's Influence Over Holmes.

Holmes and Defendant Vigman are, and were since 1966, extraordinarily close.[1] Both Holmes and Vigman described their relationship as one of "friends" (Holmes, p. 1199; Vigman p. 196).[2]

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[1] Holmes was introduced to Vigman in 1966 by Vigman's friend, Murray Silvershein, President of MHS, Inc. (Holmes, p. 1154). Vigman introduced Holmes to nearly all of the people involved in the manipulation. At that time Lugo was working in the back office at Vigman's brokerage firm and had worked for Vigman since high school (Eiseman, pp. 29-30, 11/22/85). Holmes first met Lugo when Lugo was working for Vigman (Lugo, p. 701). Vigman introduced Blumenthal to Holmes (Blumenthal, p. 962). Vigman introduced McNeil to Holmes (McNeil, p. 107). Vigman introduced Holmes to Diamond (RFA 251). Diamond met both Holmes and Blumenthal at a social function at Vigman's home (Diamond, pp. 34, 54). Vigman also introduced Lugo to Garrity in 1966 or 1967 (Garrity, pp. 21-23, 12/16/80). Lugo introduced Garrity to Holmes (RFA 574).

[2] The two have met in Las Vegas approximately 40-50 times over the past twenty years (Vigman, p. 160; Holmes, pp.

(Continued on following page)

The relationship went far beyond friendship. Holmes considered Vigman his financial advisor (Holmes, pp. 35-37) and Holmes admits that he has used Vigman as his "financial sounding board" since 1967 (*Id.*; Vigman, pp. 201-203; 216).[3]

A much sharper image of Vigman's control and influence over Holmes is shown by Michael Porter's[4] testimony of a March 1980 meeting with the two concerning the CD-3000. Porter was introduced to Vigman by Holmes as Holmes' "financial consultant, best friend and

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1326-1327). Holmes has paid several social visits to Vigman from Florida to California (Vigman, pp. 198-199) and Holmes was a guest at Vigman's daughter's wedding (*Id.*). Defendant Jack Haber also met with Vigman and Holmes in Las Vegas (Vigman, p. 159). Blumenthal met Vigman and Holmes in Las Vegas (Vigman pp. 494-495; Blumenthal, p. 264). Diamond Met Blumenthal in Las Vegas (Diamond, p. 55).

[3] Vigman has also been Holmes' financial "source." Holmes has borrowed substantial sums of money over the past twenty years from Vigman on at least three occasions (Holmes, p. 2451). These include loans of approximately $150,000 and $63,000 (Holmes, pp. 1275-1278). Holmes never paid Vigman any interest for the loans (Holmes, p. 3199). Vigman also arranged a loan for Aero Systems at the Bank of America (Garrity, pp. 32-33, 12/16/86). Vigman guaranteed a loan for Holmes (Vigman, p. 521). As Vigman said, if Holmes had wanted to borrow $50,000, and had Vigman had it, it would be "fine with him" (Vigman, p. 524).

[4] Michael Porter is a partner in the financial public relations firm of Porter, LeVay & Rose. (Porter, p. 6) As explained below, Porter, LeVay & Rose was the financial public relations firm for Aero Systems beginning in early 1980.

director" of Aero Systems (Porter, pp. 35-36).[5] Vigman did not deny it (*Id*). Vigman took control of the meeting and "it was as if Vigman was the resident genius" (Porter, p. 36). Vigman told Porter at the meeting that he was Holmes' "confidant[e]" and that Holmes "really would not make a decision without first talking to Vigman." (Porter, p. 36).

Vigman claims to have never been paid by Holmes for any of Vigman's financial advice (Vigman, p. 203). However, since about February, 1987, Vigman has been paid $5,000 per month by Hierax, a subsidiary of Aero Systems, ostensibly for introducing new products to the subsidiary (Holmes, p. 1267, 1269; 1684-1685; Vigman, pp. 272-274). This *de facto* annuity is not the only manner in which Vigman, Vigman's relatives and Vigman's companies have been paid off by Holmes for many years as will be shown below.

The pattern of racketeering between 1979 and 1981 resulting in the demise of FSSC and Sebag was a repetition of previous similar conduct and predicate activity under RICO.

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[5] Holmes' representation was untrue. Vigman never has been an official member of Aero Systems' Board of Directors. However, as the facts show, Vigman has assumed the role and has acted as a *de facto* member of the Board, without Vigman's influence on Holmes being disclosed to the public.

2. The Development of the Holmes-Vigman Relationship.

   a. J.C. Roberts and Aero Systems' Initial Public Offering.

At the time of their first meeting in October 1966, Vigman was president of J.C. Roberts & Co., a registered securities broker-dealer located in Miami, Florida (Holmes, p. 1132).[6] Although Homes didn't really need the money from a public offering of Aero Systems stock (Holmes, p. 1156), it was Vigman's recommendation to nevertheless "go public" with only 100,000 shares. The number "just felt right" to Vigman (Holmes, p. 1156).

Thus, J.C. Roberts acted as underwriter for the initial public offering of Aero Systems stock at $3.00 per share in March 1967 (Holmes, pp. 1146, 1244). It was Vigman who decided on the price per share (Holmes, p. 1159), and Vigman had full control of the 100,000 shares offered for sale (Holmes, p. 1161). Thereafter, J.C. Roberts made a market in Aero Systems (Vigman, p. 455). More importantly for Vigman, it was he who would reap windfall profits from the public offering.[7]

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[6] Lugo was employed by Vigman at J.C. Roberts first as a cashier and later in charge of the "back office;" Lugo was introduced to Holmes by Vigman. (Holmes, p. 1146; Vigman, p. 29-30). Holmes also met Elliot Eiseman during this same period of time (Holmes, p. 1147).

[7] During the processing of the Aero Systems initial public offering in February of 1967, and before the stock was offered to the public, Vigman and J.C. Roberts came under the scrutiny of the SEC for fraudulent trading practices (Vigman, pp. 653-658; Exh. 6579). The SEC alleged the manipulation of the

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The Aero Systems prospectus, as originally drafted, provided for J.C. Roberts to receive warrants to purchase 25,000 shares of Aero Systems stock as additional underwriter's compensation (Exh. 5290) (Vigman, p. 687). However, the Florida Securities Commission refused to approve the additional underwriting compensation shortly before the offering date (Metzger, pp. 113-117; Exh. 6581). The prospectus was amended to provide for a sale of the warrants to the public (*Id.*)[8]

Although strictly prohibited from receiving any Aero Systems warrants as additional compensation, Vigman did so anyway. Vigman distributed the warrants to friends and trusted customers who agreed to sell the warrants back to Vigman at or near their original cost (Vigman, pp. 689-702). Vigman was able to acquire 124 warrants for approximately $10-15 per warrant (Exhs. 6590-6591). At the time that a market for the Aero Systems warrants was established approximately one year later, Vigman sold the warrants through Executive Securities for an astonishing $894,000. (Vigman, p. 730, Exh.

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stock of Franklin Balmar, Inc. during the period from July 1964 to April 1965. Pursuant to this investigation, Vigman agreed to be barred from engaging in the securities business and from associating with any broker-dealers in August 1967 (Exhs. 6567; 6568). Notwithstanding that Holmes was put on notice of this, and clearly understood the potential adverse consequences (not to mention Vigman's questionable character), Holmes continued Aero Systems' initial public offering through Vigman and J.C. Roberts (Holmes, pp. 1185-1190; Exh. 5302).

[8] After Aero Systems' initial public offering, J.C. Roberts made a market in Aero Systems (Vigman, p. 455)

6591). Unfortunately for Vigman, the deception was uncovered and he was indicted for the warrants distribution in the Southern District of Florida (Exh. 6580). Vigman pled *nolo contendere* and was found guilty of 10 counts of securities fraud, but Vigman was fined only $100,000 (Vigman, p. 721; Exh 6585). Thus, Vigman's profit from Aero Systems warrants, *after* the fine, exceeded $790,000.[9]

Before the initial public offering, Holmes participated in a separate deceptive scheme to get Aero Systems shares into the hands of Vigman or those he controlled.[10] At Vigman's recommendation (Holmes, p. 1179), Holmes ostensibly sold 20 shares of stock to Joseph Vigman,[11] and claims to have sold 19.75 share to MHS, Inc. (Holmes, p. 1217, 11. 15 - p. 1218, 1. 13; Exhs. 5294)[12] A subsequent split of 1:800 in Aero Systems stock turned the 20 shares "held" by Joseph Vigman to 16,000 shares and MHS, Inc.'s alleged holdings of 19.75 shares to 15,800 shares. (Holmes, pp. 1220-1221; Exh. 5294). The Aero Systems stock sold to Vigman's brother and MHS, Inc.[13] was

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[9] No direct evidence of Holmes' foreknowledge of Vigman's felony has been established to date. However, because of the "sales" of Aero Systems shares to Joseph Vigman and MHS, Inc., described and because of the relationship of Holmes to Vigman, it could easily be inferred that Holmes knew what Vigman was doing.

[10] Vigman made a habit of having stock he owned and controlled in the names of others.

[11] Joseph Vigman was Vigman's brother (Holmes, p. 1179).

[12] These sales represented 14.79% of Aero Systems' outstanding stock at the time (Exh. 5294).

[13] The address of MHS, Inc. was the same as J.C. Roberts' address (Exh. 5291). MHS, Inc. became a wholly owned subsidiary of Aero Systems (Exh. 5262, at page 12).

purchased for $.50 a share (Exh. 5294); the public offering, only four months later was for $3.00 per share (Exh. 5302)[14] The preliminary prospectus filed on 1-18.67, only two and a half months later, established the $3.00 price per share (Exh. 5290). This represented a huge profit for whoever really purchased the stock at a bargain price.[15]

Despite Holmes' testimony that MHS purchased the stock (Holmes, pp. 1217-1218) and despite the fact that Aero Systems prospectus recited the same (Exh. 5297), Murray H. Silvershein, President of MHS, Inc. denies that the purchase by MHS, Inc. ever took place (Silvershein, pp. 10-11; .56; 58). Also Joseph Vigman recalls *nothing* about the transaction (Joseph Vigman, pp. 43-44).[16]

Vigman admits that he later received MHS, Inc.'s 15,800 shares of Aero Systems stock, but claims to have negotiated a sale of the shares from MHS, Inc. to his wife,

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[14] With J.C. Roberts and Vigman as the market maker, the price of Aero Systems stock went from $3.00 at the "public" offering to $135.00 per share on October 11, 1968. The high bid for that day was 27 and high ask was 27½, but taking into account a 1:5 stock split in November 1967 (Holmes, pp. 2433-2436; Exh. 3932) the original share was worth $135.00 (Exh. 4115).

[15] If sold at the $3.00 offering price, the real owner of the stock would have received $40,00 for 16,000 shares and $39,500 for 15,800 shares.

[16] The prospectuses (Exhs. 5297, 5298, 5300 and 5301) say nothing about Holmes' sale to Joseph Vigman. If indeed the stock went to Seymour Vigman, it should have been disclosed as additional compensation to the underwriter.

Nettie Vigman (Vigman, pp. 834-835; Exh. 6592)[17]. However, Silvershein unequivocally testified that he has never seen the alleged "bill of sale" from MHS, Inc. to Nettie Vigman (Silvershein, p. 61; Exh. 4109). The document, signed by Nettie Vigman, did not have an authentic MHS, Inc. letterhead, and Silvershein testified that nothing ever went out to MHS unless it was under MHS' letterhead, and that he had no knowledge of who generated the "bill of sale," (Silvershein, pp. 58, 61). Silvershein further testified that he never sold stock to Nettie or Seymour Vigman and that he never received any payment from them by cash or check (Silvershein, pp. 58-60).

From the foregoing, it is more than reasonable inference that at least the 15,800 shares of Aero Systems purportedly "sold" by Aero Systems to MHS, Inc. did *not* go to MHS, Inc. as directed in the prospectus, but went directly to Vigman as additional compensation. Thus, Vigman, who had been denied the opportunity by the Florida Securities Commission to obtain additional compensation through the warrants, obtained additional compensation through this deception.[18]

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[17] Vigman maintained complete control over Nettie Vigman's trading and stock interests. He testified that he controls "[a]nything that has to do with stocks or anything that has to do with financial, all her affairs" (Vigman, p. 27).

[18] It is also a fair inference that Holmes participated in the sham. Holmes, prior to the public offering, had owned and controlled all of the stock of the company; would he not be vitally interested in who controlled 14.79% of his stock? Holmes does not recall ever meeting or seeing Joseph Vigman (Holmes, pp. 1223-1224). Vigman was the one who probably

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Even assuming MHS was sold the Aero Systems stock as Holmes claimed, Aero Systems failed to disclose to the public that MHS, Inc. received its Aero Systems stock as a "finder's fee-type compensation" (Holmes, pp. 1226-1227; Vigman, pp. 835-836). This fact should have been disclosed in the Aero Systems Prospectus, but was not (Exhs. 5297, 5298, 5300 and 5301).

Prior to his felony conviction in Miami, Florida, Vigman moved to Newport Beach, California. (Vigman, p. 92). Undaunted by the fact that Vigman was barred by the SEC from acting as a broker-dealer and that Vigman was a felon convicted of illegally profiting from Aero Systems securities, Holmes kept in touch with Vigman after the move (Holmes, p. 1193), and continued to use Vigman as a business confidante and financial advisor (Vigman, pp. 199; 205; Holmes, p. 37). By necessary inference, Holmes saw a future of opportunity to profit by Vigman's ingenious stock schemes in the future.

D. LUGO'S CLOSE RELATIONSHIP WITH HOLMES AND VIGMAN

Lugo first met Robert Holmes in connection with the Aero Systems underwriting by J.C. Roberts in 1967 (Holmes, pp. 138: 2584-2585; Lugo, p. 701). Thereafter, Lugo operated the "back office" at Executive Securities

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recommended to Holmes the sale to Vigman's brother and to Vigman's friend Silvershein. (Holmes, pp. 1179; 1180). Finally, the fact that Joseph Vigman has such a complete lapse of memory leaves his *bona fides* in serious question.

(Winkler, p. 14). While Lugo was involved with Executive Securities, he was disciplined and suspended by the SEC.[19] In 1975, following his suspension, he formed First State Securities Corporation ("FSSC") in Miami, Florida (Exh. 8003). He met with Holmes on May 20, 1976 to discuss "what FSSC can do" for Holmes (Exh. 3950). Holmes opened various accounts at FSSC (Holmes, p. 1551). Holmes referred his mother, father, brother and his two sons to Lugo, who opened accounts for each of them at FSSC (Holmes, pp. 2922, 2921, 2918, 2910, 2903). Holmes' wife Marjorie, also opened an account with Lugo (Holmes, p. 2912). The Holmes and the Lugos met socially on several occasions, beginning in 1974 or 1975 (Holmes, pp. 151; 2426 – 2427).

As a market maker in Aero Systems (Holmes, p. 150), Lugo visited the Aero Systems premises (Holmes, p. 192) and, by 1979-1980 Holmes considered Lugo to be an "expert" in the valuation of Aero Systems stock. (Holmes, pp. 157-159; Exh. 5206). Their close relationship was typified by Holmes' identification of Lugo as "Joey" (Holmes, pp. 138; 153; 2608-2612; Exhs. 5205, 6131, 3952, 3953).

Lugo's relationship with Vigman was just as close. Vigman was Lugo's best man at Lugo's wedding (Vigman, pp. 91-92). Lugo displayed photographs of Vigman

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[19] In connection with the SEC's investigation of Executive Securities and, *inter alia*, the "spin-off" corporations, Lugo was barred from association with any broker-dealer or investment advisor with the exception that after one year he could become associated in a back office capacity and after three years he could become associated in any capacity.

in his den (Garrity, p. 28, 12/16/86), and named Vigman the Godfather of his first child (Vigman, p. 86). Vigman provided Executive Securities and Lugo access to all J.C. Roberts books and records – at no cost (Vigman, pp. 651-652). Lugo assisted Vigman's scheme to profit from Aero Systems warrants, providing the names of Lugo's relatives for use as nominees and later selling the warrants for Vigman through Executive Securities (Vigman, p. 697),[20] and through two banks that dealt with Executive Securities (Vigman, pp. 674-675). Vigman maintained an office on the premises of Executive Securities despite the fact that he lived in California and had been barred by the S.E.C. from associating with any brokerage firm (RFA 608).

E. EXECUTIVE SECURITIES CORPORATION AND NEWPORT SECURITIES

1. Lugo and Executive Securities Corporation Replaced J.C. Roberts.

Immediately after the demise of J.C. Roberts in 1967 there arose in its place -literally – a broker/dealer firm under the name of Executive Securities, founded by former J.C. Roberts employees, Lugo, Elliot Eiseman ("Eiseman") and Hal Winkler (Winkler, pp. 13-14). The firm began doing business in the same offices which had been occupied by J.C. Roberts (Metzger, p. 25) and hired a staff consisting of J.C. Roberts, ex-employees (Winkler, p. 18).

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[20] Vigman testified that Lugo's mother, aunt and uncle were among those who bought and returned warrants to Vigman. Lugo, he said, may even have contacted his relatives for Vigman (Vigman, pp. 697-699).

Executive Securities also maintained a majority of the customer accounts from J.C. Roberts (Winkler, p. 18) and made a market in the same stocks as J.C. Roberts (Metzger, p. 24, 25 and 154 also Winkler, pp. 21-26). As Jordan Metzger, the lawyer for Executive Securities put it, "J.C. Roberts subsequently became Executive Securities." (Metzger, p. 24).

Holmes, involvement with Executive Securities was substantial. Holmes had a personal account there (Holmes, p. 1194; RFA 246) and admits that he may have talked to Vigman about Executive Securities (Holmes, p. 2540-2541). Executive Securities became an Aero Systems market maker immediately after J.C. Roberts was put out of business (Holmes, p. 1191; RFA 242). On February 28, 1968, Holmes sold 25,000 Aero Systems shares to Executive Securities for $3.00 per share. (Holmes, pp. 2444; 2448-2450).[21]

The success of the Aero Systems public offering in March, 1967 was followed in January, 1968 when Executive Securities conducted an initial public offering of its own stock (Exhs. 2549; 6414) and Holmes became a substantial stockholder in the brokerage firm itself (Holmes, pp. 2537-2538; Exh. 3945). Holmes also subscribed to a private placement of Executive Securities in February 1968, a month after the first public offering of the stock (*Id.*).

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[21] On the same day, Holmes sold Nettie Vigman 50,000 shares of Aero Systems stock for $2.00 per share (Holmes, pp. 2441-2443). Holmes had approached Vigman to sell him the stock (*Id.*, p. 2445) and Holmes gave it to him for two dollars per share "[b]ecause I liked him" (*Id.*, p. 2447).

a. The Spin-Off Transactions

Holmes and Vigman "engineered" a series of corporate "spin-off" transactions by which Aero Systems stockholders received as dividends shares of Aero Systems, subsidiary corporations. The result of these spin-off transactions was to create instant public corporations whose stock could be traded in the marketplace (Exh. 6455). The investing public, who were buying these stocks in the marketplace, did not have the benefit of disclosures which would have been required under the Securities Act, and which presumably would have affected their desire to buy, sell or hold the stocks (*Id.*). Because no SEC disclosure filings were made in connection with the spin-off corporations, the prices of the stocks could be set almost arbitrarily by the market makers. Not surprisingly, Executive Securities immediately made a market in the stocks of the spin-off corporations and began trading the stocks to the public. (Metzger, pp. 154; 172-173; Exh. 6455)

Between 1967 and 1969, Aero Systems spun off securities in subsidiary companies, including Aero Tech, Hydro Tech and Micro Tenna Corp (Exh. 6455). In each instance, a public market was instantly created, J.C. Roberts or Executive Securities acted as a market maker (Metzger, p. 154), no registration statement was filed with the SEC, and shares in the newly-traded securities were distributed to Holmes and Vigman in accordance with their stock interests in Aero Systems. (Vigman, p. 505; Exh. 6455).

In his testimony, Vigman admitted that he may have recommended the spin-offs to Holmes, and that he was

involved with the spin-offs (Vigman, pp. 478-481; 497-502; 504-507). He discussed the merits of the spin-offs with Holmes. (Vigman, pp. 478-481). Holmes, likewise, admits that Vigman was involved with the spin-offs, as well as the acquisition of Aero Systems' subsidiary corporations. (Holmes, pp. 1272-73, 3296, 3308.) The flurry of spin-off transactions in the late 1960's included companies other than Aero Systems. Of significance, International Book Corp. spun off its subsidiary, Corporate Enterprises, a company formed upon the recommendation of Vigman. (Holmes, p. 3278; Vigman, p. 500; Exh. 6455).[22] Thereafter, Corporate Enterprises spun-off defendant Bunnington Corporation (Diamond, pp. 47-48; Vigman, p. 501). Holmes purchased Corporate Enterprises stock from a member of the Vigman family (Holmes, p. 3283). Also, because Holmes had purchased Corporate Enterprises stock with money borrowed from Vigman (Holmes, pp. 1276-1277), Holmes received stock in Bunnington. As with the other spin-offs, public trading commenced, no registration statement was filed with the SEC, and the stocks of Corporate Enterprises and Bunnington were placed in the hands of Vigman and Holmes, among others (Exh. 6455).

The rapid succession of spin-off transactions did not go unnoticed by the SEC. A SEC investigation resulted in

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[22] Corporate Enterprises was a company "with no activities" (Blumenthal, p. 25.). Blumenthal, who was President of Corporate Enterprises for a period of time, could not even recall the nature of Corporate Enterprises, business in the 1960's. (Blumenthal, pp. 24-25).

SEC administrative findings in 1972 that Seymour Vigman had violated the Securities Act of 1933 and the Securities Exchange Act of 1934 in connection with the spin-off transactions. (*In the Matter of Seymour Vigman*, Exhibit 6579)[23]. In accordance with his consent agreement, Vigman was "barred from being associated with any broker, dealer or investment advisor." (*Id.*) Executive Securities and the principals of Executive Securities also consented to remedial sanctions. (Exh. 6455.) Under the terms of that consent, Executive's registration as a broker/dealer was temporarily suspended, and Joe Lugo was barred from association with any broker/dealer or investment advisor "except that Lugo may after one year become so associated in a 'back office capacity' and after three years from the bar become so associated in any capacity" (*Id*).[24]

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[23] In the findings and order imposing remedial sanctions, it was found that Vigman "offered, sold and delivered common stocks of Aero Tech, Inc., Instrument Technology Corporation, Audio-Visual International Corporation, Hydro Tech Corporation, Micro Tenna Corporation, Plastic Universal, Inc., *Bunnington Corporation*, Resort Car Rental Systems, Inc., *Aero Systems*, Inc., and *Osrow Products, Inc.*, when no registration statement under the Securities Act was filed or in effect as to such securities and, in connection with transactions in such securities, quoted the securities at arbitrary prices and failed to disclose material information concerning the reason for their disposition and the persons in control, business operations and financial condition of the issuers." (Exh. 6579) (emphasis added).

[24] Defendant Martin Blumenthal was also investigated by the SEC and consented to an order barring him "from acting as or being associated with any broker, dealer or investment adviser." (*In the Matter of Martin Blumenthal*, Exh. 4826.)

Despite the sweeping investigation by the SEC concerning the spin-offs, Holmes claims to have only a "vague recollection" that Lugo and Eiseman were accused of distributing unregistered securities in the spin-off corporations. (Holmes, pp. 2577-2578.)

By 1975, Executive Securities had encountered other problems and was liquidated under the authority of the Securities Investor Protection Act (Declaration of John Moelter ¶ 2).

b. Newport Securities

Shortly after Vigman moved to Newport Beach, California in 1968, a brokerage firm named Newport Securities, Inc. commenced operations in Newport Beach, California (Holmes, p. 143). Two of the three founding principals of Newport Securities were Martin Susson and Gurdon Wolfson. Martin Susson was an insurance salesman from Philadelphia with no previous experience in the securities industry (Holmes, p. 1196). More importantly, Susson was also Vigman's brother-in-law, a fact known to Robert Holmes (Holmes, p. 145).

Gurdon Wolfson was the Chief Operating Officer at Newport Securities (Joss, p. 24), having worked previously at both J.C. Roberts and Executive Securities (Holmes, p. 1192; Winkler pp. 177-178). Wolfson, who had been Vigman's neighbor and friend in Florida (Holmes, pp. 144; 1193), became Holmes' personal stock trader at Newport Securities. Holmes did not give any particular reason why he, a Florida resident, opened a securities account with a California brokerage firm (Holmes, pp. 143-145). Of course, Seymour and Nettie Vigman also had

accounts at Newport Securities (Vigman, p. 179). As one would expect, Newport Securities became a market maker in Aero Systems stock (Holmes, pp. 1193-1194).

Although Vigman had been barred from associating with any broker/dealer, he played a role in both the creation and operation of Newport Securities. Vigman testified that Susson and Wolfson met with him "accidentally" in Newport Beach prior to the formation of Newport Securities. (Vigman, pp. 467-468).

Susson stated that Vigman arranged for him to leave the insurance business in Philadelphia to become an owner of Newport Securities (Susson, p. 27-28). Garrity testified that before Newport Securities opened, he met with Vigman at the Doral Hotel in Miami, Florida (Garrity, pp. 8-12, 12/6/86), where Vigman brought up the subject of whether or not Garrity would be interested in joining Newport Securities when it opened (*Id.*, 12/16/86) Garrity, at the time, declined to do so (*Id.*, 12/16/86).

Joss testified that Vigman controlled Newport Securities (Joss, pp. 21-22). Joss further testified that Wolfson had told Joss that Vigman was involved in Newport Securities (*Id.*, p. 22).[25] Joss also attended a meeting with Vigman and Wolfson at Vigman's home at the time that

[25] As described, Wolfson and Vigman were co-conspirators in the manipulation of stock prices in DCS Financial Corporation. Joss' testimony is thus admissable under Federal Rule of Evidence 801.

the SEC ordered Newport Securities to shut down and liquidate its inventory (*Id.*, pp. 24-25). At this meeting, Vigman discussed the stock positions that Newport Securities held in inventory and how they would be liquidated (*Id.*, pp. 25-26).

Joss further testified that there was another meeting that he attended in the early 1970's held in Palm Springs, California, which Vigman, Wolfson, Susson and Garrity attended. (*Id.*, pp. 27-28.)[26]. The purpose of the meeting was to "promote" a stock in which Newport Securities made a market (*Id.*). According to Joss, both Wolfson, who revered Vigman's "genius," and Susson stated that Vigman had the ability to "engineer" corporations, *i.e.*, creating enough of a facade for people to get interested in buying a stock (*Id.*, pp. 49; 59-63). Newport Securities, along with other market makers, would have the ability to raise a stock's price whereas a single broker could not (*Id.*, pp. 59-64).

Thus, Holmes' close friend and advisor Seymour Vigman was, in effect, an insider at Newport Securities, the west coast market maker for Aero Systems. Newport Securities fared no better than Executive Securities in avoiding the scrutiny of the SEC in connection with unlawful trading practices.

[26] Garrity later became a broker at Joseph Sebag, Inc. He was introduced to Joss as an employee of Newport Securities while Joss was visiting the Newport Securities' offices. (Joss, pp. 31-32).

F. THE FSSC – SEBAG RELATIONSHIP

1. The Formation of FSSC

After Executive Securities ceased doing business in 1975, Lugo and Eiseman formed FSSC (Eiseman, p. 100, 5/7/86). At the time, Lugo still had two months left on a SEC suspension from being associated with a broker dealer (Eiseman, p. 102, 5/7/86).

Eiseman and Lugo were the only two shareholders of FSSC (Eiseman, p. 105, 5/7/86). Eiseman was FSSC's President; Lugo was Vice President, Treasurer and financial principal (*Id.*, 5/7/86) He also was in charge of all back office operations, and he also attempted to develop a retail clientele (*Id.*, p. 124, 5/7/86). Lugo was responsible for the preparation of the monthly Focus Report (*Id.*, pp. 126-127, 5/7/86). Although Eiseman signed the monthly Focus Reports as President, he did not review them. In fact, he did not understand the source for the entries made in the reports or understand the calculations contained in the reports (*Id.*, pp. 128-129, 5/7/86).

2. Vigman Introduced Lugo to Garrity

Garrity originally met Lugo while visiting J.C. Roberts & Co. in the late 1960's (Garrity, p. 14, 12/16/86). Vigman reintroduced Garrity and Lugo in 1976 or 1977 (*Id.*, p. 21, 12/16/86) and told Garrity that Lugo had opened FSSC (Garrity, p. 74, 2/29/88). The Lugo-Garrity relationship would continue until the collapse of FSSC and Sebag.

Lugo introduced Garrity to Aero Systems, Aerosonic, Bunnington, Creditbank, Dash and Osrow. Lugo encouraged Garrity to retail the stocks to his customers (Garrity, p. 54, 2/29/88). He provided Garrity with information concerning Aero Systems, Aerosonic, Bunnington, Creditbank, Dash and Osrow (Garrity, p. 53-54, 2/29/88). Lugo called Garrity often at the office and at home (Garrity, p. 68, 2/29/88).

3. Lugo, Garrity and Aero Systems

Garrity first became aware of Aero Systems in the late 1960's (Garrity, p. 183, 3/2/88). Garrity ceased to be interested in the company some time around 1970 because Aero Systems had no earnings (Garrity, pp. 187-188, 3/2/88). He had no interest in Aero Systems again until late 1976 or 1977 when he bought a few shares from Lugo (Garrity, p. 183, 3/2/88).

Garrity became active in Aero Systems again in early 1980 (Garrity, p. 185, 3/2/88). Lugo was a significant factor in Garrity's decision to resume an interest in Aero Systems (Garrity, p. 228-229 3/2/88). During a visit in 1980, Garrity, Lugo and Lewis Leeds[27] met with Holmes at the Aero Systems facility (Holmes, p. 2379). Lugo set up the meeting between Holmes and Garrity (Holmes, p. 2381). Garrity followed most of Lugo's suggestions (Garrity, p. 230, 3/2/88).

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[27] Leeds had been the president of International Book, one of the spin-off companies that Vigman brought public in the 60's. Leeds later opened his own stock brokerage firm (Garrity, pp. 230-232, 3/2/88).

Prior to the announcement of the acquisition of the CD-3000 in April 1980, Garrity was led to believe that there was going to be an announcement that would be exciting with the investment community and "make the stock go up." (Garrity, pp. 210-211, 230-231, 3/2/88). After the announcement, and when Garrity began retailing the Aero Systems stock, he repeatedly told his customers about the CD-3000 (Garrity, p. 194, 3/2/88).[28] Garrity heard "grand and wonderful things" from Lugo and Vigman with respect to Aero Systems selling fuel management systems (Garrity, p. 36, 12/16/86).

From early 1980 through July of 1981, Aero Systems was "highly liquid" as a result of numerous announcements about the CD-3000 (Garrity, pp. 33-35, 3/1/88). There was a lot of buying activity and Garrity built up a position in the stock (Garrity, pp. 33-35, 3/1/88).

In 1980-81, Garrity liquidated his position in Aero Systems into the market created by Robertson Securities purchasing the stock (Garrity, pp. 190-191, 3/2/88).

4. Lugo, Garrity and Bunnington

Another of the companies that Lugo introduced Garrity to was Bunnington (Garrity, p. 84, 2/29/88). Garrity caused Sebag to make a market in Bunnington (Garrity, pp. 52-53, 2/29/88).

In the later part of 1976 and early 1977 Vigman, Blume' ıal, Speyer[29] and acquaintances of Vigman began

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[28] Sebag was a market maker for Aero Systems at all times between February, 1980 and July, 1981 (RFA 921).

[29] Ron Speyer is Vigman's son-in-law (Vigman, p. 13).

to trade the stock of Bunnington through accounts at FSSC (Eiseman, p. 342-367). During that time period, Vigman related entities purchased or sold 152,000 shares of stock (Exhs. 6625, 6626).

Due to the questionable nature of the purchases and sales of Bunnington stock through FSSC, the trading of Bunnington was investigated by the NASD (Eiseman, pp. 342-367, 5/8/86). Based upon the NASD investigation, a disciplinary action was instituted against Lugo alleging that he manipulated the price of the Bunnington stock (Eiseman, p. 345). Lugo was censured and fined (*Id.*, p. 365, 5/18/86).

G. THIS RISE AND FALL OF DCS FINANCIAL CORPORATION

Vigman and Diamond incorporated DCS Financial Corporation ("DCS") in June, 1972 by Vigman and Diamond with a $500,000 investment from Vigman and a $500,000 senior subordinated convertible debenture purchased by Nettie Vigman (Diamond, p. 92; Exhs. 2835 and 6593). Diamond later purchased 160,000 shares of DCS on August 29, 1972 (Diamond, pp. 103; Exh. 6593). In addition, Blumenthal also purchased 20,000 of DCS on the same date (Exhs. 2836; 6593).

In a complex transaction in September 1972, DCS merged with El Chem Machinery and, through a subsequent plan of reorganization, El Chem's public shares were reduced through a 1-for-7 reverse split. El Chem issued 700,000 new shares, of which Vigman ultimately controlled 500,000 shares. (Exhs. 2837, 2852). At the completion of this reorganization, Vigman and Diamond

became the two largest shareholders (Diamond, p. 126). The reorganization also created a public market for DCS and eliminated the company known as El Chem Machinery, Inc.

Vigman, Diamond and Gerald Fincke, a lawyer, were the only members of the Board of Directors of DCS (Exh. 1059 at p. 13). Once Vigman and Diamond gained control of DCS, and it became a publicly traded company, its stock price rose dramatically. In less than 3 months, the stock price rose from 25 cents bid/50 cents ask ($1.75 and $3.50 adjusted for the reverse split) to $39 bid/$41 ask (Exh. 2852). Newport Securities was the principal market maker for the DCS stock during this period (Combs, p. 24).

Once again, the SEC began to investigate and, on November 29, 1972, issued an order stopping the public trading in DCS stock (Vigman, p. 897; Exh. 8000). The SEC thereafter brought a civil action against Newport Securities, its principals, DCS, Vigman and Diamond (Exh. 2852). Prior to trial, Vigman entered into his third consent agreement with the government, this time enjoining him from engaging in fraud in the purchase or sale of securities. (Vigman, p. 897) After a trial in 1973 before the United States District Court for the Central District of California, Judge W. Matthew Byrne, Jr. entered findings of fact supporting the issuance of a permanent injunction against DCS, enjoining it from further violations of the Securities Act of 1933 and the Securities Exchange Act of 1934 (Exhs. 2852; 5406).

Although the SEC's stop trade order was subsequently lifted, the permanent injunction had a substantial

impact on the ability of DCS stock to be traded and for DCS to find market makers (Diamond, pp. 238-39). The price of DCS stock dropped very dramatically after the SEC trading ban went into effect (Diamond, p. 1071) and, despite the fact that Diamond and Fincke persuaded Vigman to resign as an officer and director of DCS (Fincke, pp. 74-75),[30] DCS stock prices languished and there was virtually no public market for the DCS stock after the 1973 injunction (Diamond, pp. 1071-72).[31]

At first, Diamond and McNeil considered having Bunnington purchase DCS in order for Bunnington to acquire Springwater as an asset (Fincke, p. 82). McNeil wanted Bunnington to own Springwater very much

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[30] Gerald Fincke, the lawyer for DCS testified that the principals of DCS wanted to get rid of the company in a two step process. First, Fincke recommended that the principals (*i.e.*, Diamond, McNeil and Fincke) get rid of Vigman in an attempt to make DCS a "financially real public company" because Vigman's reputation with respect to securities matters was so bad (Fincke, pp. 74-75). Fincke testified that "the obvious manipulation of DCS' stock" while Vigman was in control just added to it (*Id*). Fincke did not believe that anybody would treat it as a real company as long as Vigman was associated with it (*Id*). Thus, he and Diamond persuaded Vigman to resign from DCS (*Id*). Second, Fincke and Diamond realized that the company was winding down, served no purpose because of financial reasons and had a large net operating loss carry forward. (*Id*).

[31] Vigman supposedly "sold" his DCS stock in August 1973 to Nettie Vigman, Speyer, Diamond and Arvin Grossman. The "sale" to Speyer was a sham. Also McNeil testified that he purchased 40,000 shares of DCS from Vigman in 1974 at $.25 a share (McNeil, pp. 47-53; 59-61).

(*Id.*).[32] However, they learned that there was no way to structure the transaction by which Bunnington could obtain DCS's operating loss carry forward because of the common control situation with Diamond's positions in both Bunnington and DCS (Fincke, p. 80).

Being unable to acquire the company they wanted "very much," Holmes, Vigman, Diamond and McNeil developed a much more profitable plan that gained them Springwater and valuable Aero Systems stock.

H. DCS MERGED WITH AERO SYSTEMS

Holmes, Vigman, Diamond and McNeil conceived and executed a scheme to get tradeable Aero Systems securities in the hands of DCS shareholders and to get Springwater, DCS, only viable asset,[33] back to Bunnington. Vigman, not DCS officers Diamond or McNeil, initiated merger discussions with Holmes in 1976 by which DCS would be acquired by Aero Systems (Holmes, p. 1381, Vigman, pp. 286; 291; 771).[34]

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[32] Diamond, President and Chairman of the Board of Bunnington, was responsible for managing Springwater's operations (Holmes, p. 170).

[33] Exh. 5308, pp. 001-12225 and 001-12252

[34] At the time the negotiations commenced with Holmes in 1976, Vigman was not on Bunnington's Board of Directors, nor was Vigman a large shareholder of Bunnington (Holmes, p. 1272). Shortly after the merger, Vigman became a substantial shareholder of Bunnington, and then Springwater was sold back to Bunnington by Holmes. Vigman eventually not only had valuable Aero Systems stock but also control over Springwater, the only viable element of DCS the ruination over which he had presided.

Holmes discussed the terms of the merger with Vigman (Holmes, p. 2941; Exh. 4049; Diamond, p. 298) and "kicked . . . around" the exchange of DCS stock for Aero Systems stock (Vigman, p. 291), the consideration for the merger (Vigman, p. 796), and participated in the negotiations regarding the merger (Vigman, p. 752). Vigman also discussed the proposed merger with Diamond and McNeil after his initial discussion with Holmes (Vigman, pp. 775; 786). Holmes asked Lugo to render an opinion as to the value of the Aero Systems stock and FSSC did so (RFA 843).

Tom Huston, Vigman's personal accountant and the accountant for J.C. Roberts[35] told Holmes before the merger that the IRS would disallow DCS' loss carry forward if the principal purpose of the acquisition was the reduction in income tax and that the companies should " . . . well document the business reasons for the transaction and that you be aware that the Internal Revenue Service has this very potent weapon if it challenges the use of the loss carryover" (Exh. 5314)

Aero Systems and DCS followed Mr. Huston's advice. They each prepared a list of "reasons" for the merger (Exhs. 5315, 5317). Conspicuously absent from either list was the use of the tax loss carry forward. Yet Diamond admits that Holmes, and Aero Systems' reason for the DCS merger was because Aero Systems had the ability to use the tax loss carry forward that DCS brought

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[35] Vigman referred Huston to Holmes (Vigman, p. 782). He also referred Huston to Diamond (Vigman, p. 783).

with it (Diamond, p. 1075). This reason for the merger remained undisclosed to the public or the IRS.

On the other hand, 18 of the DCS shareholders had compelling reasons to accomplish the merger (Exh. 5315); they would receive restricted but eventually tradeable, Aero Systems stock for their DCS stock (Diamond, p. 1072).[36]

Since at the time of the merger there was very little trading in DCS stock (Diamond, p. 1071;) DCS pronounced what was the single, true and only reason for the merger. In its Information Statement Concerning Special Meeting of Shareholders of DCS Financial Corporation held on June 27, 1976 it said:

> "Secondly, for the past three years there has been no public market for the Company's Common Stock; therefore the merger will enable all shareholders owning what is theoretically, but not in actuality, freely tradable stock to receive cash for an illiquid investment considerably in excess of (4 1/2 times) its book value."

The Statement continued:

> " . . . [o]n the other hand, even though these shareholders will receive in the merger

[36] The merger agreement was signed on July 22, 1976 (Exh. 1066). It was between DCS and Aero Systems Avionics, Inc., a wholly owned subsidiary of Aero Systems (RFA 125). The terms of the merger included, *inter alia*, that Avionics would acquire all of the DCS common stock in exchange for 939,461 shares of Aero Systems common stock and $32,000 in cash (RFA 147). Holmes and Diamond structured the deal so that only 18 "major" shareholders received Aero Systems stock for their holdings in DCS while the other 377 shareholders only received the $32,000 cash (Exh. 5315).

> restricted Aero shares which will not be saleable to the public for at least two years, they will nevertheless own stock in a profitable publicly traded company which, if they so desire, may in the future be sold in the public market pursuant to Rule 144." (Diamond, p. 1063; Exh. 5315)[37]

At the time of the merger in 1976, the following were among the DCS shareholders who would receive Aero Systems stock: Nettie Vigman – 106,925 shares[38] Speyer – 106,925 shares,[39] Diamond – 595,289 shares and Blumenthal – 24,863 shares (Diamond, pp. 1076-1077; Exh. 5316).

Diamond, the Chairman of DCS at the time of the merger (Diamond, p. 1063) acknowledged that the exchange of untradable stock for tradable stock (after a holding period of two years) was a benefit to him and he did consider this fact in deciding whether or not to sell DCS to Aero Systems (Diamond, p. 938).

[37] This statement was distributed to DCS shareholders concerning the merger (Diamond, p. 1065).

[38] Nettie Vigman is Vigman's wife and Diamond's sister (Diamond, p. 1007). Vigman has admitted that his wife knows nothing about any of the stock transactions and that he controlled all of the stock in her name (Vigman, p. 27).

[39] Vigman claims that Speyer bought 90,000 shares of DCS stock from Vigman in 1973 for $104,000 (Vigman, p. 13). Speyer sold 50,000 shares of Aero Systems stock in September, 1980 (Exh. 9001) (after the manipulation had caused a rise in the stock price) and Vigman claims to have split the proceeds among Vigman's four children (Speyer, p. 14; Vigman, p. 17). However, in truth all but $44,125 of the $237,500 was deposited – under Vigman's handwritten endorsements – to Nettie Vigman's account in November, 1980 (Vigman, pp. 20-25; Exhs. 9007-9009).

Before the merger, Holmes knew that Diamond was the largest single shareholder of DCS[40] and that Diamond's son would also receive 24,440 shares in the merger (Holmes, 2959-2960; Exh. 5316). Indeed, Holmes knew that Diamond would own approximately 12% of Aero Systems stock in the event that the merger went through (Holmes, pp. 3025-3033; Exh. 5316), and that Blumenthal would receive 24,863 shares (Holmes, p. 1470; Exh. 5316). Holmes knew Nettie Vigman had DCS stock at the time of the merger (Holmes, pp. 1443-1446).

Significantly, Aero Systems' Notice of Annual Meeting of Shareholders with Proxy Statement dated and mailed July 2, 1976 (Exh. 4075) relating to shareholder approval of the merger did not mention the fact that Vigman, or Nettie Vigman, or any of Vigman's family, including Speyer, would end up owning Aero Systems stock if the merger was approved by the shareholders. Yet Holmes admitted that he knew that to the extent that the merger agreement called for Aero Systems shares to be issued to the Vigmans, they would end up with a substantial portion of Aero Systems (Holmes, pp. 3025-3032). Vigman, through his wife Nettie and other family members he controlled, together with Diamond and his son, ended up with 17% of the company (Holmes, pp. 3030-3036).

Holmes, following Huston's advice, extolled to his public the "business" benefits that justified the merger

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[40] Diamond owned 55% (Exh. 5315; RFA 818). He voted all of his stock in favor of the merger (RFA 820).

(Exh. 5317)[41] But despite his public posture, Holmes *failed to disclose* that he had *no interest in keeping Springwater* (Diamond, pp. 1074-1075).[42] This fact supports the clear inference that Holmes' motives, and those of his co-conspirators, were not just to sell DCS to Aero Systems.

After the merger, rather than take an active role in the management of Aero Systems's new acquisition, Holmes left the responsibility to Diamond (Holmes, pp. 170; 215). Further, after the merger, Diamond became a director of Aero Systems in July 1976, Treasurer of Aero Systems in August 1976, a director of Aero Systems Avionics Corp. (an Aero Systems subsidiary), President of

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[41] It stretches logic to believe, in the first instance, that a Miami, Florida airplane "junk dealer" would be interested in a Rochester, New York machine shop; no common product, no relationship of product or business.

[42] This publicly undisclosed disinterest is clearly supported by the fact that only eleven months after the "merger" was completed in July 1976 (Exh. 5325), Holmes and Diamond approached the Southeast Bank (which held Aero Systems' line of credit) in June, 1977 to get the bank to waive its security agreement and allow Aero Systems to sell Springwater assets to Bunnington (Holmes, p. 1601; Exh. 5333) However, Southeast Bank would not waive its security agreement or permit the sale to take place (Holmes, 1601; Exh. 5333). Springwater was making money for Aero Systems that year. Springwater generated more earnings than the balance of Aero Systems (Holmes, p. 1601). Since one of the "business" reasons for the merger Holmes told his public was that it would add to Aero systems' profit picture, why sell it at all? Indeed, the fact that Holmes sold it, and the timing, strongly infers an understood pre-arrangement to get it back – in the hands of those at Bunnington who wanted it originally but couldn't have it.

DCS, Chairman of Springwater and Chairman of Bunnington (Holmes, pp. 1490-1491, 1497, 3118; Exh. 4092; RFAs 311, 325, 328, 876, 881, 882). In addition to these rather comprehensive ties between Holmes and Diamond, Holmes also gave Diamond a "consulting agreement" with Aero Systems which Holmes believes was signed shortly after the merger (Holmes, pp. 1610-1612; Exh. 4098).

I. VIGMAN'S ENTRY INTO BUNNINGTON

Once Vigman and Diamond had successfully rid themselves of the worthless DCS stock, obtained a substantial interest in Aero Systems stock and put the only profitable DCS asset, Springwater, into the hands of their good friend Holmes (with the understanding that Bunnington would get it back), Vigman dramatically entered Bunnington Corporation.

In May 1977, Vigman sold 160 acres of land in California to Bunnington for 405,084 shares of Bunnington stock (Exh. 7301). By virtue of this, Vigman became the largest Bunnington shareholder, a director of Bunnington and served as chairman of Bunnington's Executive Committee (Exh. 1572). Before Vigman bought his Bunnington stock, Diamond and McNeil eagerly wanted Vigman to join them and discussed various alternatives of getting Vigman to join them. (Exh. 1574).[43]

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[43] Of course, this eagerness does not square with Fincke's and Diamond's expressed reservations about Vigman's "bad reputation" and his connection with DCS. It strongly infers

(Continued on following page)

J. SPRINGWATER WAS SOLD BACK TO BUNNINGTON

1. Vigman, McNeil and Diamond Finally Reacquired Springwater Through Bunnington Which They Could Not Do Through DCS

Now that Vigman had become a substantial shareholder of Bunnington, the final phase of the DCS/Aero Systems merger was played out. Springwater found its way back to Messrs. Vigman, Diamond and McNeil under Bunnington's roof – a result they could not have achieved without Mr. Holmes and Aero Systems.

During the time that Springwater was "owned" by Aero Systems, Diamond was an Aero Systems officer and Board member (Diamond, p. 303) and received financial information concerning Springwater (Diamond, pp. 312-313). Also, Diamond ran Springwater on a day to day basis after the merger (McNeil, p. 1108). Diamond, in addition to sitting on Aero Systems's Board and being Aero Systems's Treasurer, served as a consultant regarding Springwater (Holmes, p. 170) assisted Aero Systems in obtaining loans from banks (Holmes, pp. 170; 214; 1498-1502), obtained financing for Springwater from two Rochester Banks (Holmes, p. 214) and served as "Special Assistant to the President/Financial Planning" regarding Aero Systems (Holmes, pp. 171-173; Exh. 5207).

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that Diamond and McNeil's efforts to have Vigman "resign" from DCS was so that potential purchasers of DCS, such as Holmes, would not have to disclose Vigman's association with DCS to his shareholders.

After the merger, McNeil, who was the President of Bunnington Corporation and served on its Board of Directors (Exh. 1572 on p. 03633, 1591), was also on the Board of Directors of Springwater (McNeil, p. 1093).

After the abortive attempt by Bunnington to get Springwater back to the fold in 1977, efforts were renewed in early 1978. (McNeil, p. 289). Vigman admits that he "probably" participated in discussions with McNeil, Diamond and Holmes regarding the purchase price of Springwater by Bunnington (Vigman, pp. 795-796). Holmes admits it is more than likely "he discussed it with Vigman." (Holmes, p. 1590-1591) McNeil negotiated on behalf of Bunnington, and he made the details of the "negotiations" known to Vigman and Diamond (Diamond, p. 308; McNeil, p. 290)[44]

Effective March 1, 1978 Springwater's net assets were sold to Honeoye Industries, Inc., a wholly owned subsidiary of Bunnington (RFAs 150, 151; Exh. 1068)

Bunnington's press release concerning the sale was brief (McNeil, pp. 350-351; Exh. 1593). Both the press release and Bunnington's letter to its shareholders (Exh. 1592) did not disclose the obvious conflicts of interest

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[44] In a memorandum from Diamond to Vigman dated May 19, 1977 (Exhibit 2862) regarding what had to be done to accomplish the Springwater to Bunnington transaction, Diamond wrote "Aero Systems has to provide absolute minimum." Diamond testified that it may have meant in terms of cost of preparation (Diamond, pp. 314-315). It is also consistent with Holmes and Aero Systems already having done enough as accomplices to complete the plan of getting tradable stock into the hands of Vigman and his compatriots, and Springwater back to them.

which existed by virtue of the multiple roles played by Diamond and McNeil both as officers and directors of the acquired and acquiring companies and Aero Systems, nor did it describe Diamond's and McNeil's roles in the "negotiations," nor Diamond's extensive shareholdings in Aero Systems. It didn't even disclose the company from which Bunnington purchased Springwater (*Id.*). Diamond testified that there was never any consideration given to the type of reporting that would be required to shareholders and to agencies about the inter-corporate relationships (Diamond, p. 286). This is despite the fact that the direct question of conflict of interest had been raised by Diamond's bankers in 1977 (Diamond, pp. 1075-1076). Diamond claims that the question was resolved by advice of counsel (*Id.*), but McNeil says he didn't discuss the conflict with Fincke, the company's attorney (McNeil, p. 352). Fincke himself recalls no discussion regarding the need to disclose the conflicts or from what company Bunnington purchased Springwater (Fincke, pp. 206-207; 209; Exh. 1501).

Perhaps the best reason for Bunnington's cryptic notice to shareholders was given by the attorney, Fincke. He said that if Bunnington had revealed who the seller of Springwater was, Bunnington could not have stopped there, but would have to go back to DCS and go back to Vigman to get into the whole relationship (Fincke, pp. 210-211). Of Course, that's the last thing that Holmes, Vigman, Diamond and McNeil wanted to do.

Holmes' accommodation of his friends at Bunnington doesn't stop simply with the retransfer of Springwater into their hands. The terms by which it is done reveal that Bunnington off-loaded California Leisure Corporation

stock, a Bunnington subsidiary, onto Holmes and Aero Systems as a major part of the Springwater/Bunnington deal.

The sale of Springwater to Bunnington was ostensibly for $600,000. (Holmes, pp. 2961-2964; Exh. 4055). $250,000 in cash was paid by Bunnington and Bunnington signed a note to Aero Systems for $350,000 (*Id.*). The note was secured by California Leisure Products stock (*Id.*)[45] One payment of $50,000 was made against the note leaving a balance of $300,000 owed by Bunnington to Aero Systems (Exh. 8002 on 446-15408). Then, in October, 1978 Holmes purchased from Bunnington 47,500 shares of California Leisure Products for $1.00 per share (Holmes, pp. 2215-2216; Exhs. 3896 and 3897), and he had Aero Systems buy 110,000 shares of the same stock from Bunnington at the same price (Holmes, p. 2217-2218).[46] Bunnington intended to use the monies it received from Holmes and Aero Systems to partially pay off the installment contract with Aero Systems for the sale of Springwater, and Holmes knew it (RFAs 807, 825).

Thus, Holmes had Aero Systems accept $300,000 cash for Springwater and then paid Bunnington $157,500 of

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[45] Bunnington owned 86% of California Leisure at the time (Holmes, p. 1607-1608; Exh. 5334).

[46] Holmes became President or Chairman of California Leisure (Holmes, p. 2662) and discussed it with Vigman before he did so (Holmes, p. 2679). Although Holmes claims he'd had no prior dealings with Vigman's son-in-law, Ronald Speyer (Holmes, p. 2678), Holmes asked Speyer to be on California Leisure's Board of Directors (Holmes, p. 2676-2677). California Leisure was not much of an "investment" for Aero Systems shareholders. Aero Systems had to write down Aero System's investment in it (Holmes, p. 2681).

capital by buying the very California Leisure stock (or its equivalent) that secured the debt and allowing Bunnington to "pay" more than half of the existing debt to him and Aero Systems.

Since the valuable Aero Systems' stock was restricted, the DCS players had to wait at least two years before they could begin selling it.

K. THE CD-3000 WAS USED BY HOLMES, VIGMAN AND OTHERS BY USE OF FALSE STATEMENTS, TO CREATE INVESTOR INTEREST IN AERO SYSTEMS

The DCS players had had to wait at least two years to have realistically marketable Aero Systems stock. Aero Systems stock bumped along at an average of $1.34/bid/$1.50 ask in 1977, $3.59 bid/$3.75 ask in 1978 and $2.70 bid/$3.08 ask in 1979. (Foley Decl. ¶133)

1. Aero Systems Acquired the "World Wide Marketing Rights" to the CD-3000

The CD-3000 "Fuel Management Computer" was designed as a "pilot aid" (Hayden, pp. 17-18) for general aviation aircraft operators (*e.g.*, twin Cessnas, commuter planes, etc) (Hayden, p. 21). The CD-3000 was not originally designed as a fuel savings device (Hayden, p. 134), despite the fact that Holmes built an advertising campaign around the device as a system for saving fuel (Hayden, p. 136).[47] In fact, the CD-3000 displays gross

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[47] Hayden thought of the device more of a range extender than as a fuel savings device (Hayden, pp. 134-135). Thus, the CD-3000 wasn't "designed" to "save fuel" as Holmes claimed later.

aircraft weight, fuel remaining, and is not a "computer" in any real sense. The CD-3000 is no more useful for fuel saving than an aircraft manufacturer's performance chart (Davies, pp. 149-150).[48]

Holmes claims that he first heard about the CD-3000 from Charles Hayden ("Hayden") of Colt Electronics, Inc. ("Colt") in February or March 1980 (Holmes, pp. 10-12).

Holmes had a "personal desire" to do something with the CD-3000 (Holmes, pp. 29-30).[49] Vigman shared Holmes' enthusiasm for the CD-3000 (Holmes, p. 31). Holmes discussed with Vigman the possibility of merger between Aero Systems and Colt (Holmes, p. 16). However, Vigman advised Holmes not to buy Colt, but to purchase the rights to the CD-3000 instead (Holmes, p. 30).

Holmes made a trip to Colt in March 1980 (Holmes, pp. 16-17), and told Vigman he was going (Vigman, p. 424).

Robert Lynn, President of Colt, went to Florida after Holmes "invited him to come down" to "discuss some things that might be of interest" (Lynn, pp. 69-70). On March 26th, 1980, the day Lynn arrived in Miami, Holmes showed him around the Aero Systems premises (Holmes,

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[48] Continental Airlines' pilots rejected the CD-3000 since "the computer wasn't doing anything different than what one of the flight crew members would do with a calculator" (Kightlinger, pp. 29-30).

[49] It is the opinion of John Torkelsen, one of plaintiffs' experts, that the stock of Aero Systems was manipulated (Torkelsen Decl. ¶16).

p. 34; Lynn, pp. 71-72; p. 87). The following morning, Holmes took Lynn to Vigman's apartment (Lynn, pp. 70-72; 85-86). Vigman knew Holmes wanted Lynn to meet Vigman (Vigman, p. 423). Prior to this meeting, Holmes had mentioned the CD-3000 to Vigman (Vigman, p. 423). Holmes introduced Vigman as "one of his advisors or something." (Lynn, p. 70). Holmes and Vigman told Lynn about their long term relationship, and Vigman acted as a character witness for Holmes (Lynn, pp. 79-80). They described to Lynn how completely they trusted each other (*Id.*). Subsequent to this meeting, Holmes notified Vigman that Holmes had made the deal with Colt for the marketing rights to the CD-3000 (Vigman, p. 455).

On March 27, 1980, before Lynn left Miami, Holmes signed a letter of intent between Aero Systems and Colt regarding the CD-3000 (Lynn, pp. 85-86; Holmes, p. 40; Exh. 5201). On April 22, 1980 a definite agreement was signed between the two companies (Holmes, pp. 91-92; Exh. 5202).[50]

2. The proper market for the CD-3000 was limited to business jets

The CD-3000 was the idea and invention of Hayden, employed by Colt (Hayden, p. 17). Hayden was an experienced business jet pilot and had a lengthy history in the aircraft industry (*Id.*, pp. 11-18). He had been a member

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[50] Colt extended the original exclusive agreement through 1986, and he "thinks" for an additional two years in 1986. Colt didn't renew the agreement thereafter (Holmes, pp. 3062-3066; Exh. 4082).

of the National Business Aircraft Association since its inception in 1949 (*Id.*, p. 261).

Hayden handled the marketing for Colt (*Id.*, pp. 137-138). He believed the market for the CD-3000 would be small (*Id.*). He believed that the market was very limited for other than business jets (*Id.*, p. 69). Further, Hayden believed the CD-3000 was not of practical use in the general aviation field (*Id.*, p. 69).[51] Hayden was aiming at the business aircraft market (*Id.*, pp. 21-22). He wanted to keep the price low enough to attract commuter aircraft and he did not believe that the CD-3000 would ever be a seller in the airline market (*Id.*). He did not pursue the airline market because he saw no potential for sales in it (*Id.*, pp. 139-142). He had looked at the airlines and found a complete lack of interest (*Id.*). He had conducted market studies by conversing with pilots from all over the world (*Id.*, p. 52). Hayden estimated that Colt would get CD-3000 sales involving 10% of the existing executive aircraft in operation, and approximately 25% of the new executive type aircraft being sold (*Id.*, pp. 53-54). The estimate was based on his examination of the market and of the planes in the market (*Id.*). He estimated that sales would be 35-50 per year (*Id.*).[52]

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[51] The term "general aviation aircraft" refers generally to all aircraft other than commercial aircraft. (*See* Hayden, p. 69).

[52] Hayden's forecasting proved both right and wrong. First, he was right about the market; only 7 were sold by Holmes to airlines between April 1980 and December 1987 and *none* were sold to general aviation aircraft (Exh. 5285). Hayden was wrong, however, about how many would be sold. In eight years, Aero System sold only *90* CD-3000s, which is only a little over *11* per year – less than one a month (Exh. 5284).

Holmes told Hayden how much he wanted to market the CD-3000 under the Aero System's name (*Id.*, p. 61), and that Holmes had expressed that he thought it "would be a great thing for the airlines" (*Id.*, p. 64).[53] However, Hayden told Holmes before Holmes acquired the rights to the CD-3000 that he (Hayden) did not think it would ever be a big seller (*Id.*, p. 137). Hayden expressed extreme skepticism about the arrangement (*Id.*, pp. 61-62). Hayden told Holmes in 1980 that Airlines' maximum efficiency occurs at between Mach .74 and .76 but that airlines operate between Mach .80 and .82 despite fuel considerations (*Id.*, p. 144). Hayden told Holmes that airlines know how to save fuel but don't because of time constraints and that sales to airlines "was a complete and total dead issue." (*Id.*, p. 144; 267-268).[54] Also, Lynn told Holmes that the application of the CD-3000 was limited to business jets, and was only "remotely" applicable to commercial aircraft (Lynn, p. 91). When Holmes sensed Hayden's unenthusiastic reception, Holmes offered Hayden 5,000 shares of Aero Systems stock "if you don't raise too much fuss with Bob (Lynn) to go ahead with this." (Hayden, p. 62)[55].

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[53] Holmes admits that before he signed the agreement with Colt, no CD-3000 had been sold to any commercial airline (RFA 260).

[54] Holmes admits that Hayden "may" have told Holmes that the commercial airlines were not the proper market for the CD-3000 (Holmes, p. 284). Holmes admitted that international airlines were his principal target (Holmes, p. 113). He also admitted that he knew that the device could not be sold to single engine planes (Holmes, pp. 85-86).

[55] While Aero Systems' files are replete with "incentives" or "inducements" to airlines to buy or test the device (facts

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Aside from the idea of selling to the airlines, Holmes never expressed a marketing concept to Hayden except that Holmes intended to sell through dealers (*Id.*, pp. 69-70).

Indeed, before Holmes acquired the "worldwide distribution rights" to the CD-3000 he had had no market study done (Holmes, p. 43).[56] Holmes could have cared less; the real reason that Holmes wanted the rights to the CD-3000 was best expressed by Holmes to Hayden when Holmes was trying to induce Hayden to accept 5,000 Aero Systems shares for not raising a "fuss": "Mr. Holmes expressed to me that, *when he made his pitch with all his people, that the stock would go up sharply*" (Hayden, pp. 179-180) (emphasis added).

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which are too numerous to detail here, but facts with which Aero Systems will not disagree), the bribe to Hayden is only one of two actual known bribes made by Holmes in his desperate efforts to sell the CD-3000 to an airline. In the late spring of 1982, Holmes attempted to bribe Frederick Lind, the Vice President of Engineering and Quality Assurance of Continental Airlines, to enter into "a joint advertising campaign" (Lind Declaration). While this occurred after collapse of the brokerage houses, it is compelling evidence to show that the airlines had not been the proper market, and that Holmes knew it.

[56] Holmes testified that he didn't need a market survey (Holmes, p. 2077). He should have done one, a point that is made quite clearly by Robert Litle, "Special Representative, Aero Systems Aviation Corp" in his memorandum to Holmes dated August 21, 1981 (Exh. 3869). Litle told Holmes that he has "continued my market analysis of airline customers" and that, while the survey "is not yet complete" fully 65% out of 407 aircraft "cannot be fitted with the CD-3000 at this time" (*Id.*). Litle joined Aero Systems on June 21, 1981 (Exh. 8005); was with Aero Systems for two years and his title was approved by Aero Systems (Holmes, p. 2082).

Holmes, however, didn't listen, didn't investigate the market and didn't care what the inventor knew the market for the CD-3000 to be. He had a different agenda.

3. Holmes, Vigman and Others Started to Make the "Pitch" and Misrepresented the Capabilities and the Market of the CD-3000

a. Holmes and Vigman Immediately Began Selling the Device to the Stock Market: They Used Porter LeVay & Rose

Rather than immediately investigate the market for the CD-3000 because of Hayden's caution, or even try to sell the device to the airlines, Holmes and Vigman immediately set out to "sell" the CD-3000 to the stock market.

Holmes first met Mike Porter of Porter, LeVay & Rose ("PLR")[57] sometime between November-December 1979 and January 1980 (Porter, p. 10). Aero Systems retained PLR in or about February, 1980 (Porter, p. 10,) for the express purpose of getting publicity for Aero Systems and its stock (Holmes, p. 634).

Porter was told by Holmes in early 1980 that Holmes was pursuing some new product which Holmes didn't identify (Porter, p. 22).

Holmes called Porter on March 25 or 26, 1980 and told Porter that Holmes had "finalized what they were talking about," that they had acquired "a new product" and wanted "to do a big publicity campaign and really get the story out about this new product because it was

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[57] Porter, LeVay & Rose is a financial public relations firm (Porter, pp. 6-7).

going to bring in millions and millions of dollars of sales to the company" (Porter, p. 32). Holmes asked Porter to fly to Miami right away and Porter did so on March 27, 1980 (*Id.*).[58]

When Porter met Holmes in Miami, Holmes wanted to give Porter "input for the press release" which Porter was to take back to New York and draft (Porter, p. 33). During his discussions with Porter, Holmes kept describing the "millions and millions of dollars that this was going to make and the profits that this was going to give the company and that every single commercial plane in America needed it and so do most general aviation aircraft . . . " and that Holmes "felt the *financial community would go absolutely crazy over this*" (Porter, p. 35) (emphasis added).

After the first meeting with Holmes at Aero Systems' premises, Porter was driven by Holmes to "Vigman's condo" in the Ft. Lauderdale area (Porter, pp. 32-34). On arriving at Vigman's condo, Holmes introduced Vigman as Holmes' "financial consultant, best friend and (as a) *director* . . . [o]f Aero Systems" (*Id.*, p. 35-36) (emphasis added). Vigman didn't deny it (*Id.*). Vigman took control of the meeting "as if Vigman was the resident genius" (*Id.*). Vigman told Porter that he, Vigman, was "Bob Holmes' confidant, if you will, and that Bob (Holmes) would not make a decision without first talking to Vigman" (*Id.*, p. 36). Vigman also warned Porter that he,

[58] This is the same day that Lynn was in Miami and signed the letter of intent.

Vigman, "was chairman of the Bunnington Corporation . . . ," that "he had hired PR firms before" and that "he (Vigman) knew (Porter's) business" (*Id.*, pp. 36-37).[59]

The meeting with Vigman and Holmes took an hour and a half to two hours (*Id.*, pp. 38-39). The three discussed PLR's distribution procedure and what PLR was going to do with the press release (*Id.*, p. 38). While Holmes did contribute to the conversation, Holmes sat back and mostly listened to Vigman talk (*Id.*, p. 41). Vigman also commented that he was "a substantial shareholder in Aero Systems and was looking for the stock to really be a super duper stock with a sensational growth company" (*Id.*, p. 39). Holmes and Vigman were "absolutely just 'blue skying' how terrific this piece of machinery was . . . " and discussed that if "Eastern put the CD-3000 on all of their planes it would save them millions and millions of dollars . . . " (*Id.*, pp. 37-38).

b. Vigman Was Heavily Involved With Holmes in the Promotion and Publicity Program for the CD-3000

PLR started its publicity campaign for Holmes.[60] Its activities included, *inter alia*, introducing Aero Systems to

[59] Vigman not only knew the business, but he practiced it at Bunnington, as well. Around the middle or end of 1980, McNeil told Garrity that Vigman was "the one that handles the PR end of Bunnington" (Garrity, pp. 42-43, 12/16/86).

[60] PLR's distribution process included sending all releases to the Wall Street Journal office in Atlanta to get on the Dow system, and were distributed to Reuters, the New York Times

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the financial community, preparing and distributing releases to the financial community and the business, financial and trade press, placing articles in the financial publications, arranging conferences with financial columnists, updating market makers and discussing Aero Systems with numerous members of and analysts in the financial community (Exhs. 953; 959; 971; 972; 973; 978; 991; 994; 999; 1004; 1007 and 1008).

Shortly after the first press release on April 1, 1980, Vigman and Holmes didn't like the kind of exposure the CD-3000 was getting. Porter prepared a memo to Holmes[61] as to how PLR would handle Aero Systems releases in response to Vigman and Holmes' "rather strong comments about our system, the way we were making releases, and if I am not mistaken, this was because they felt the release on the CD-3000 did not get enough pick-up in the media" (Porter, p. 58; Exh. 956).

Porter had a number of discussions with Vigman about PLR's promotion of Aero Systems stock and the CD-3000 (Exh. 953, p. 407-0098; Exh. 973, p. 407-0002).

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and onto the PR Newswire. They were also mailed out to a mailing list made up of brokers and money managers (Porter, pp. 55-56).

[61] Porter wrote Holmes that all releases were to be prepared by PLR from information supplied by Aero System, then reviewed by Aero System and released by PLR with Holmes' approval (Exh. 956). Porter testified that this procedure was followed (Porter, p. 59, ll. 16-18). Thus, PLR released nothing without Holmes' approval and Holmes is personally responsible for the releases and their content. Holmes frequently sent the releases to Vigman for review (Vigman, p. 443-444).

Vigman and Porter began to have words with each other because of Vigman's discontent with the way the material was distributed, and Porter kept telling Vigman that Vigman wasn't the client (Porter, p. 58, ll. 19-25). Vigman threatened Porter that he, Vigman, was " . . . a rather large shareholder and I have alot invested in this company." (*Id.*, p. 59).[62] Porter told Vigman that he wouldn't discuss it with him but would go through Holmes, but then things started to get rocky. Porter had problems with Holmes because of the "back-biting that Sy Vigman started to do in our firm." (*Id.*, p. 59). Holmes also told Porter that Vigman was unhappy. (*Id.*, p. 59).

After Porter told Vigman that he wouldn't deal with Vigman, Holmes called Porter and told Porter that Vigman wanted to talk to Porter about what PLR was doing

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[62] Vigman also privately told Garrity that he, Vigman, was either the first, second or third largest shareholder of Aero Systems (Garrity, p. 23, 12/16/86). Vigman privately told Eiseman that he was the largest shareholder of Aero Systems (Eiseman, pp. 79-80, 11/22/85). Plaintiffs have been unable to locate any public disclosure by Holmes or Aero Systems of Vigman's substantial stock holdings in Aero Systems, of Vigman's criminal past, of his extraordinary close association with Holmes, of his claim of being a director of Aero Systems or his pervasive control and influence over Holmes. Indeed, his shadowy presence is hidden by public disclosures to the contrary. In Bunnington's Form 8-K for March 31, 1978 relating to the Springwater sale to Bunnington, Vigman publicly disclaimed owning any Aero Systems stock and told the public that he didn't control Nettie Vigman's 206,925 shares, his two childrens' 120,000 shares or his son-in-law's 236,925 shares (a total of 11.49% of Aero Systems) (Exh. 4105). Note surprisingly, Holmes certified that the Vigmans were not a control group (*Id.*).

(*Id.*, pp. 91-92). Porter was in the position that since Holmes demanded that Porter talk to Vigman, he did it (*Id.*). Vigman wanted to know what PLR was going to do for the next several months for Aero Systems "to get the company more exposure" (*Id.*). Porter told Vigman that there were no specifics because he was waiting for dates from the financial community for Holmes to take him on the road to meet brokers (*Id.*). Vigman told Porter that he, Vigman, wanted to make sure that PLR wasn't letting down in their activity ". . . because (Vigman) *wanted the stock higher* because he thought it was worth a hell of a lot more than it was at this particular time" (*Id.*) (emphasis added).[63]

In a July 1980 conversation, Vigman told Porter that he was following Porter's activities, knew what Porter was doing and was reviewing it (Porter, p. 100). Vigman warned Porter: "I am watching what you are doing (Porter, p. 101)."[64]

c. "Friends of the Company" Assisted Holmes, Vigman and PLR

Employing the "Sponsorship" concept, Holmes used three or four "friends of the company;" a few special marketmakers that Holmes and Vigman could rely on.

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[63] Aero System's stock price had gone from a low of $2.78 bid/$3.25 ask in April 1980 to a high of $4.00 bid/4 3/8 ask in June, 1980 (Foley Decl. ¶ 135).

[64] It's very apparent that Holmes *wouldn't* move without Vigman's approval. Holmes told Porter in about July that he, Holmes, was sending copies of PLR's monthly activities reports to Vigman (Porter, p. 100; Holmes, p. 624).

Porter learned from Holmes, in conversations during the normal course of their business relationship, that there was a group of three or four people who had "been in the (Aero Systems) stock" whom Holmes considered "friends of the company" (Porter, p. 65). These "three or four" were Joe Lugo, Lewis Leeds in Florida, and Roger Garrity in California (*Id.*). Through Porter's activities on behalf of Aero Systems, he observed that the three most active marketmakers were the three; when he sent them releases, they always said who was leading the charge or who was doing what "and it always came up to those three" (Porter, pp. 65-66).[65] Porter had numerous conversations with both Lugo and Garrity and talked on a "fairly regular basis" (Porter, p. 86; Exh. 972, pp. 407-0019, 0020; Exh. 973, p. 407-0002; Exh. 978, p. 407-0313; Exh. 999, p. 407-0280).[66] Porter observed that the three were "so involved in the company" (Porter, p. 86), and he would send kits of materials out to various people at Lugo, Leeds and Garrity's request (Porter, p. 124).

Holmes' relationship with Lugo appeared to affect Porter's ability to do his job, or made his job superfluous. Porter testified that Lugo always had the Aero Systems

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[65] An analysis of Lugo's trading clearly shows Lugo's domination of the market on days when Vigman, Speyer, Diamond, or Holmes sold into the market place (Foley Decl. ¶ 124).

[66] In June 1980, Porter reported to Holmes that he'd had numerous conversations with Lugo and Garrity, and that each held a position of 900,000 shares of Aero System stock (Exh. 972).

information before Porter did (Porter, p. 88).[67] Despite the fact that PLR would make a release, but didn't know exactly when the release went out, Holmes felt that the release was out and let the people in his close group know what was going on: "That was the way (Holmes) operated. He always had this close group of bond people that he knew" (Porter, pp. 176-177).

Garrity told Porter that he "talked to Lugo constantly. That was their network. They knew what was going on on a day to day basis with each other" (Porter, pp. 88-89). Garrity also told Porter that he, Lugo and Leeds talked to Vigman frequently (Porter, pp. 87-88).

The relationship between Aero Systems and PLR deteriorated and Holmes dismissed PLR on April 20, 1981 (Exh. 1009). Porter had become increasingly concerned with AERO Systems's inability to meet its earnings projections (Porter, p. 135). Holmes had continued to refuse to give PLR statistical information regarding the CD-3000, including test information, test results and where they were selling the units (Porter, pp. 103-104).[68] A lot of reporters kept requesting the additional information from

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[67] There's a clear inference that Lugo was operating on insider information from Holmes.

[68] This is hardly surprising. As of March 31, 1981, Holmes admits that he had not received any written test results from *any* source regarding the CD-3000's performance (RFA 939). Holmes didn't *have* any written test results reported until July, 1981 (Holmes, pp. 44; 1910-1911; Exh. 1039). Further, only 10 CD-3000's had been sold by the date of PLR's dismissal (Exh. 5284). For Holmes to disclose the truth of the number of sales to the financial press would have been devastating to his stock price.

PLR, but PLR had no way of getting it because Holmes wasn't being responsive and simply kept putting off supplying the information (Porter, pp. 103-104).

Porter testified that the split between PLR and Holmes was caused by, among other things, a personality problem between corporate officer (Holmes) on the one hand who started the company with his bare hands and believes what he's doing, and a public relations person who, above all, believes in credibility and feeding proper information to the financial community (Porter, pp. 200-202). Porter wanted information to come out on what was actually going on *vis a vis* Aero Systems's projections (*Id*). Most significant however, is Porter's statement that "[t]here was, if you will, a behind-the-scenes force going on there just by Mr. Vigman in whatever they were doing together as far as operating this company, and their philosophy certainly differed from mine" (*Id.*, at 202). Garrity was a little more direct on the rift; Porter told him that Porter felt Holmes lied to him (Porter) about the CD-3000 (Garrity, pp. 40-41; 265-268).[69]

2. Holmes, Vigman and Porter, LeVay & Rose Issue False Press Releases

a. April through June 1980

Holmes was responsible for the preparation, content and distribution of Aero Systems' press releases (Holmes,

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[69] There is a strong inference that Holmes and Vigman didn't need PLR anymore. Between September 1, 1980 and the time PLR was discharged (April 20, 1980), Vigman, Speyer and Holmes had already sold 296,925 shares of Aero Systems stock for $1,796,499 (Foley Decl. ¶ 134).

p. 3025). Nothing went out from the company without Holmes' approval (*see* fn. 61, *supra*). Holmes discussed press releases with Vigman (Vigman, pp. 443-444); he sent press releases to Lugo (Holmes, pp. 109-276). There is no evidence anywhere that Holmes ever modified, changed or retracted any press release, news article, quotation, shareholder letter, annual report or other public document, once that item had been publicly disseminated.[70]

Holmes' very first press release on April 1, 1980 regarding the CD-3000 (Holmes, p. 658; Exh. 947) states that "The potential market for this much needed new product includes all multi-engine jet, turbo prop and piston aircraft in the word." Thus, Holmes included all of the world's airlines and all of the world's general aviation aircraft in his "potential" market, having done no market study, having no test results and having been told by the inventor that the market Holmes described to the public is not the market for the product.[71] Holmes also

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[70] Holmes testified that he tried it once, but that there's no way "to get these things changed" (Holmes, pp. 379-380).

[71] Both Vigman and Holmes gave input to Porter for the press release (Porter, p. 38). Vigman and Holmes told Porter that the CD-3000 was "designed to reduce fuel consumption by 15%" (Porter, p. 47) and was reflected in the first draft of Porter's first press release (Exh. 948). There is no basis anywhere for a claim of 15% fuel savings. In fact, at the time of the release, neither Holmes nor Colt *had* any empirical written test results concerning what or what not the CD-3000 would save (Lynn, pp. 87-88; Holmes, pp. 46-47), and Holmes knew this (Lynn, pp. 89-90). The actual first press release didn't include any reference to any alleged fuel savings. The fact that Holmes and Vigman told Porter that the device saved 15% fuel, however, clearly shows the two of them creating "percentages" out of whole cloth.

states that he plans to market through a "selective network of dealers. Holmes didn't sign up his first dealer for the CD-3000 until September 14, 1981 (Exh. 8001), eighteen months after he signed the CD-3000 agreement.

On April 23, 1980 (a day after the final agreement was signed between Colt and Aero Systems), Holmes announced that Aero Systems planned to lease the unit "to commercial and business aircraft operators . . . in exchange for a percentage of actual fuel savings" (Exh. 5203). Holmes then stated that "airlines alone will spend more than $30 billion for fuel this year" (*Id.*) The obvious effect sought was that Aero Systems would get, by its leases, that percentage of the $30 billion of fuel saved (Holmes, pp. 105-106). By analyzing Exhibit 5284 which lists all CD-3000 sales and the price paid, through November 1987, it is clear that Aero Systems never entered into any such lease. There was no public announcement that Aero Systems's "plan" was not implemented.

On April 28, 1980 Holmes prepared and sent a letter to Aero Systems' shareholders which states, *inter alia*:

> 1. "[W]e are very pleased . . . to inform you of a very exciting new development that could be the most significant event in our history."
>
> 2. "[W]e are entering an exciting new market . . . ")
>
> 3. "[P]resent business jet users have indicated fuel savings to be in the area of 10%."
>
> 4. "[O]ur initial market includes installation in the 50,000 plus multi-engine jet, turbo prop and piston aircraft currently in operation . . . "

5. "[W]e are currently discussing a leasing proposal with one of the major air carriers . . . in exchange for a percentage of actual fuel cost savings."

6. "[T]he potential savings could be a fantastic amount since the world's airlines are expected to spend more than $30 billion for fuel this year, a third of that amount by the U.S. Airlines."

7. "[W]e are thrilled with the added potential of this exciting new high technology product that could be greater than everything we have done throughout our entire history." (Holmes, p. 108; Exh. 5204)

The non-existent "market" identified by Holmes consisted of over 50,000 aircraft of all kinds through the world. There are no facts that Holmes possessed that every aircraft in the world could or would use the CD-3000.[72] Holmes testified that he merely pulled the figure out of Jane's All the World Aircraft (Holmes, p. 109). However, there is still no support for Holmes' claim that all the world's aircraft could or would use the device (Declaration of Davies, ¶¶ 3-5). Further, Holmes doesn't disclose that Colt's capacity to produce the CD-3000 is

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[72] In fact, Davies testified that general aviation aircraft operators (*e.g.* twin piston, turbo-prop, etc.) would not be interested in the CD-3000 because of its high relative cost (Davies, p. 107), because the cost of fuel is a very small part of the cost of small plane ownership (Davies, p. 69), and because fuel quantity, fuel flow, and gross weight information is available with less expensive devices (Davies, p. 107). And, as Airlift International's Robert Sovacool observed, all new generation jets have more exotic fuel management systems as original equipment (Sovacool, pp. 24-25; *See also* Davies Declaration ¶¶ 3-5).

extremely limited.[73] Holmes doesn't disclose Colt's reservations as to the CD-3000's limited market appeal, or the inventor's warning that airlines won't use it.

i. Holmes' Claim That The CD-3000 Saved 10% Fuel Consumption Was False

Holmes' representation that "business jet users have indicated fuel savings to be in the area of 10%" was false and known to be false at the time it was published.

Holmes admits that there were no written test results of the CD-3000 before he signed the agreement with Colt (Holmes, pp. 46-47). He never received *any* written test results from anyone at Colt (Holmes, p. 48). Holmes admits that the first written test results of any tests on the CD-3000 he or Aero Systems received were in July of 1981 (Holmes, pp. 444; 1910-1911; Exh. 1039).

Holmes claims that Lynn and Hayden of Colt *told* him that fuel savings were in the area of 10% (Holmes, p. 117), and that Hayden had told him that Smith (a pilot for Landis Tool) was "getting about 10%" (Holmes, p. 120).

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[73] Lynn testified that in 1979-1980 Colt had about 10 people of whom three were in production (Lynn, p. 20). In 1980, Colt had only 7,500 square feet and "probably five" people in production (Lynn, p. 21). Colt maintained a "very small" inventory of three to five CD-3000s, and after the Aero System agreement they produced CD-3000s on an "as needed" basis (no inventory was maintained) (Lynn, pp. 57-58). It took Colt three (3) months to produce a CD-3000 from date of order and, all things being equal, Colt could only have produced "several hundred" per year (Lynn, pp. 58-59).

However, Lynn denies that there are or ever were any empirical test results from the CD-3000, or that he every gave any to Holmes (Lynn, pp. 110-111). Lynn doesn't even recall any customer telling him that there was a percentage fuel savings by using the CD-3000 (Lynn, p. 31). Lynn never even knew of a percentage savings or fuel maximization, nor did anyone else to his knowledge (Lynn, pp. 28-29). As Lynn stated: "We have no idea what the fuel management computer can save a person in economy" (Lynn, p. 28). Lynn does not recall any discussions with Holmes or Vigman during his March 1980 trip to Miami related to percentage of fuel savings, and at that time there were no test results (Lynn, pp. 87-88). Hayden does not remember "ever saying 10%" (Hayden, p. 42).

Lynn says that Hayden was bandying about the 10% savings numbers, but that there was no test data to support it (Lynn, pp. 89-90), and if percentage figures were passed on to Holmes, Holmes was told that there was no test data to support them (Lynn, p. 101). Lynn further testified that any percentage figure was "pure speculation" and Holmes was told that it was (Lynn, pp. 100-101).

Smith (a pilot at Landis Tool, one of the two business jet operators who had installed the CD-3000 before Aero Systems entered into the agreement with Colt) never represented to anyone at Aero Systems or to anyone on behalf of Aero Systems that fuel savings were possible with the CD-3000 (Smith, p. 40). As a matter of fact, Landis Tool bought the device because it provided more information; they did not buy it to conserve energy, and never used it to conserve energy (Smith, pp. 45-47).

There is no evidence anywhere that Holmes obtained testimonials from "business jet users" that the device saves 10% of fuel before Holmes made that claim in his public announcements.[74]

ii. Holmes Failed To Disclose Significant Limitations On The CD-3000's Capabilities And Usefulness

Holmes also failed to disclose to the public the technical capabilities, or lack thereof, of the CD-3000. Holmes failed to disclose that:

(1) Reservations expressed by the inventor and manufacturer regarding the market Holmes was claiming (Hayden, pp. 21-22; 141; Lynn, pp. 90-91);

(2) The use of the CD-3000 is very limited. The CD-3000 only is capable of use on the "cruise" portion of the flight, and thus the interest of any airline depended on the "block times" of the airlines' flight schedules.[75]

(3) At the time of the agreement between Colt and Aero Systems, the CD-3000 was not capable of being used on aircraft weighing over 100,000 pounds. (Lynn, pp. 114-116) and was not

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[74] The totality of the shareholder letter is not only abnormally hyperbolic, but gives the potential stock purchasers the distinct impression that Aero Systems, by its "leasing" arrangement to a U.S. airline, would garner earnings equivalent to at least 10% of 10 billion dollars (one third of the $30 billion spend on fuel by the world's airlines).

[75] (Hayden, pp. 267-268; Exh. 2406).

available in a model for such use until six (6) months after the agreement was signed (*Id.*).[76]

(4) Prior to the sale of the CD-3000 the FAA had to issue a Supplemental Type Certificate ("STC") for use of the device on any given type aircraft for which it was purchased. (Sovacool, p. 56). From the time of the application until the STC is obtained can be from three to six months (Hayden, pp. 34-35).[77]

(5) The use of the device would slow a commercial jet down and that commercial airlines, as Hayden warned are tied to a tight schedule and would not adopt a device that interfered with that schedule;[78]

(6) Use of the device depended heavily on pilot acceptance and, as pilot Smith said, in

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[76] Virtually all of the commercial airlines and all cargo carriers operated in the time frame from April 1980 to July of 1981 operated at gross weights in excess of 100,000 pounds. (Declaration of Davies ¶ 2). These aircraft included the following makes and models: Lockheed L-100, L-1011; McDonnell Douglas DC-8, DC-9, DC-10; Boeing 707, 727, 737, 747. *See also* Holmes Response to RFA 652. The CD-3000 couldn't be installed on aircraft in excess of 100,000 pounds until at least September, 1980 (Exh. 2413).

[77] Once an application for an STC is made, a FAA inspector must issue a Type Inspection Authorization, and then a FAA inspector has to test the unit for safety and compatibility with that specific type of plane (Hayden, pp. 30-31). After all of these steps are completed, then the FAA will, in time, issue the STC (*Id.*). Only two types of business jets had CD-3000 STC's at the time Holmes signed the agreement with Colt (RFAs 167-168). In fact, only four STC's had been issued prior to mid-1982 (Exh. 2402).

[78] *e.g.*, American Airlines advised Holmes in (August 6, 1981) that they considered time to be more critical to their operation than fuel savings (Holmes, p. 2154; Exh. 3882).

order to utilize the device, one would have to operate outside the flight manual; "Flight manual is Bible. You don't ever do that" (Smith, pp. 36-38);[79]

(7) The lack of capabilities of Colt to manufacture the CD-3000 in the gross numbers of the "market" that Holmes was leading the public to believe existed for the device.[80]

On the same day of Holmes' shareholder letter the same material was published by the National Quotations Bureau, Inc. (Exh. 116).[81]

On June 9, 1980, Holmes caused to be published an advertisement in Barron's which said "Initial results from business jet users indicate fuel savings to be in the area of 10%" (Holmes, p. 1695; Exh. 3806).[82]

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[79] Roy Johanson, Aero Systems' VP-Marketing, who reported directly to Holmes (Johanson, pp. 13-14), testified that the CD-3000 was less successful with airlines than business jets due to poor pilot acceptance (Johanson, pp. 77-78). Pilots were not inclined to use the CD-3000 because of their cockpit work load. Johanson discussed these opinions with Holmes, but Holmes thought he could overcome lack of pilot acceptance through "marketing" (Johanson, pp. 80-82).

[80] *See* footnote 73, *supra*.

[81] Holmes admits that he periodically sent information to the Grinde Organization (NQB publisher), but does not know if he sent this to the Grinde Organization (Exh. 116; Holmes, pp. 135-137).

[82] The use by Holmes of the plural "users" is not just disingenuous but is a deliberate misstatement calculated to deceive the public into thinking that the business jet market was crowded with the devices. Holmes only claims to have spoken to Smith of Landis Tool (*supra*, p. 62) and Lynn and

(Continued on following page)

b. July 1980

During April, May and June 1980, Aero Systems stock price remained fairly level from a low 2 7/8 bid/3 1/4 ask to 4 bid/4 3/8 ask (Foley Decl. ¶ 135). It's during this time that Holmes and Vigman were expressing dissatisfaction with PLR's program.

On July 1, 1980 PLR prepared and sent Holmes a draft of a "proposed fact file" which was "intended to outline Aero's operations succinctly for members of the financial community" (Porter, p. 74; Exh. 969). Holmes redrafted the "fact file" and sent it back to Porter (Porter, p. 76; Exh. 969, pp. 407-0563-0566). Porter redrafted it again, taking out some of what Holmes had inserted and finalized it (Porter, p. 77; Exh. 969, pp. 407-0567-0573). The "fact file" and Holmes' revisions are very significant.

First, Holmes reiterates the false claim that "initial results from business jet users indicate fuel savings to be in the area of 10%" and the false claim that the initial market for the device is "50,000 + multi-engine jet, turbo prop and piston aircraft . . . " These misrepresentations stayed in the final "fact file."

Second, Holmes added that "As of June 30, (1980) Aero Systems met the final requirement of the Federal

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Hayden of Colt (*supra*, p. 62). Smith (who denies he told Holmes anything about a 10% savings) is the *only* business jet "user who could have been Holmes' source. Further, by use of "initial results," Holmes is telling the public that there were some tests conducted on the CD-3000 giving "initial results." There were no tests and no "initial results."

Reserve Board to qualify its stock for sale on margin and expects to be included in the next qualified list to be published in October. This factor alone should greatly enhance the value of the stock" (Exh. 969 at p. 407-0565).[83] This was included in the final "fact file" except for the last sentence (*Id.*, 407-0561); while not expressly said to the public, the last sentence clearly shows that qualifying for margin was part and parcel of Holmes, Vigman and Lugo's carefully conceived plan to raise the Aero Systems stock price without any underlying economic justification.

Third, Holmes adds "We see Aero Systems as the best buy in the market today for capital appreciation and would not be surprised to see the value of this stock triple before the end of this year" (*Id.*, p. 407-0565). While this was muted substantially by Porter in the final version (*Id.*, p. 407-0573), Holmes' unsupported enthusiasm and actual motive underlying the acquisition of the marketing rights to the CD-3000 is abundantly clear.

Finally, Holmes recklessly, if not falsely, projects sales and earnings of an unprecedented and unsupportable amount attributable, in part, to the CD-3000. Porter's original draft of the "fact file" (*Id.*, pp. 407-0558-0562) says nothing about Aero Systems' earnings. In Holmes' redraft for PLR's use in the fact file (*Id.*, pp. 407-0563-0566 at p. 406-0563), Holmes wrote:

> Aero Systems Inc., is the most exciting situation that (Porter LeVay & Rose) have ever had to work with. (PLR) believe(s) the Company is on

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[83] The Federal Reserve Board approved Aero Systems' stock for sale on margin in early October, 1980 (Exh. 123).

> the verge of a major breakout in both sales and earnings, that could exceed $50 million in sales and $1.50 to $2.00 in earnings by 1983 as a result of:
>
> x x x
>
> c. Sale and lease revenues from the Company's unique new Fuel Saving Computer which potentially could dwarf the Company's entire operations.

Holmes' predictions appeared in the final "fact file" (Exh. 970, p. 407 0153).[84]

The final version of the "fact file", together with Holmes' letter to shareholders was sent by mail to approximately 5,000 members of the financial community (Porter, pp. 81-82; Exh. 970).

PLR's report had the desired effect. As Porter reported to Holmes on September 22, 1980 concerning PLR's August 1980 efforts: "The report was widely distributed . . . We have received numerous responses from the report and have seen an increase in the stocks' activity . . . *Roger Garrity* of Investors Financial Services, Inc. and *Joe Lugo* of First State Securities *both told us that the*

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[84] Aero System's *actual* sales and earnings were:

	1981	1982	1983
Sales	$14,487,016	$17,263,786	$26,918,626
Earnings	.06	.10	.21

Aero System 1983 Annual Report (Exh. 5261)

interest in the stock is being generated from the report" (Exh. 978) (emphasis added).[85]

Also, in July 1980, Holmes was interviewed by Martin Merzer of the Miami Herald and told Merzer the falsehood that "Our tests show (the CD-3000) can result in fuel savings of up to 10%" (Exh. 119; Merzer, pp. 8-9). Aero Systems had received no written test results (RFA 945).[86]

c. Holmes, Vigman and PLR Get Moore Schley to Join Their Forces and the False Releases Continue.

At the time PLR prepared and disseminated its "fact file," Holmes, Vigman and Lugo found another "friend of the company" in a small brokerage firm in New York, Robertson Securities and its clearing broker, Moore & Schley, Cameron & Co. (both referred to as "Moore Schley").[87]

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[85] During this time period, PLR, *inter alia*, prepared and distributed to the financial community at least four releases on the CD-3000 (Exh. 953, p. 407-0096; Exh. 959, p. 407-0080; Exh. 971, p. 407-0028).

[86] Aero Systems claims to have conducted tests, but the tests didn't provide any percentage of fuel savings because Aero Systems wasn't "actually using any fuel" (Holmes, pp. 185-186).

[87] Holmes opened an account at Moore Schley (Sayegh, p. 51). In November of 1980 Holmes sold 50,000 shares of his company for over $8.00 per share and received $409,095 (Exh. 3863). Vigman also opened an account for himself or his children at Moore Schley to sell a block of Aero System stock

(Continued on following page)

Messrs. Sheidy, Augus and Figliozzi of Moore Schley traveled to Miami to visit Holmes on September 16, 1980 (Sheidy, p. 57).[88] At the conclusion of the meeting, even before they returned to New York, Figliozzi or Sheidy called Sayegh, Moore Schley's trader, and told Sayegh to buy and accumulate Aero Systems stock (Augus, pp. 38-39). Only three days later, on September 19, 1980, Moore Schley issued a stock "analysis" letter prepared by Augus (Augus, p. 21) not only stating that Moore Schley was a market maker of Aero Systems but containing false and misleading statements (Exh. 117). It states that "The system has indicated, in early testing, fuel savings in the area of 10%." Augus testified that Holmes "showed us some test results" and "he went over the test results with us" and said that "early testing had confirmed it was a substantial fuel saver" (Augus, p. 55). Thus, Holmes fabricated those "test results" for Augus because Holmes has unequivocally admitted that he had received no written test results concerning the CD 3000 in September 1980 (RFA 961).

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(Vigman, pp. 266-269). Moore Schley also filled out a new customer account form for Joan Vigman, Vigman's daughter, from information provided by Holmes, the purpose of which was to allow the sale by her of 25,000 shares of Aero System stock (Sayegh, p. 68; Holmes, pp. 1074-1075; Exh. 160). Holmes introduced Diamond to Moore Schley and Diamond opened an account there in July of 1982 (Figliozzi, pp. 212-216; Exhs. 163, 164). Speyer and Michael Lipman [Vigman's son-in-law (Vigman, p. 25)] both sold 20,000 shares of Bunnington through Moore Schley in March 1982 (Figliozzi, pp. 344-346, 353; Exhs. 192-195).

[88] Before Porter had prepared PLR's "fact file," Porter had discussed Aero Systems with Moore Schley (Porter, p. 79).

Further, Moore Schley's stock "analysis" again falsely reiterates that the market for the device is "50,000 aircraft" (Exh. 117). It, like the PLR report, omits to mention any of the critical facts about the device that the public would need to know to make an intelligent decision on the purchase of Aero Systems stock.

Six days later, on September 25, 1980, Moore Schley issued another incredible Aero Systems stock "analysis" which is ten (10) pages long (Exh. 118).[89] Augus repeats the false claim about "early testing" showing fuel savings "in the area of 10%" (Exh. 118, p. 1).[90] It *expands* the false claim of the "market" for the device to "50,000 private aircraft, 5500 commercial aircraft and . . . a large number of military aircraft" (*Id.*, p. 2). Incredibly, the analysis goes on to claim (on pp. 7-8) that "this (fuel) savings varies between 4 and 16%. This has been borne out by extensive testing in the current units installed in the deHavilland . . . , Saberliner and . . . Jetstar." Augus testified that "my report [Exh. 118] was done from things that I had in my file. Whatever is in this report was in my file" (Augus, p. 138). *No* such information concerning the

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[89] Augus, who wrote the long report, says that the reason that the one page report was put out was because "the stock started to get very, very active and started to move up . . . we decided not to wait for the printer (who had the long report) . . . The stock was headed higher" (Augus, pp. 37-38).

[90] The effect on the financial community of the group's "10% fuel savings" barrage was reported to Holmes by Porter in the PLR September activity report (Exh. 991). At Exh. 991, p. 407-0325 Porter reported that a Paine Webber representative had told him " . . . that a 75 hundred dollar investment could reduce overall fuel expenditures by a minimum of 10% is 'just phenomenal'."

alleged test reports or market data was in Augus' file (Taylor Decl. ¶6). Again, there was no such written test data, let alone "extensive" test data extant at the time of this "analysis" (Holmes, p. 204, 11. 17-22; RFA 945). Finally, Holmes reviewed the September 25, 1980 Moore Schley report and provided his comments on it to Jules Augus (RFA Nos. 215, 216). Again, the report omitted the significant facts that were or should have been known to Holmes.

The evidence is clear that Moore Schley joined the conspiracy to manipulate Aero Systems' stock. Great shards of Augus' "analysis" are lifted *verbatim* from the PLR "fact file" of a month earlier (*cf.* pp. 2-7 of Exh. 118 to PLR's "fact file" Exh. 5208).[91]

Augus vehemently denies that he copied PLR's "fact file" when confronted with the identical parts of the two reports (Augus, pp. 102-150). He goes further at p. 150: "I say this unequivocally. I never dealt with Porter, LeVay relative to Aero Systems. Personally, I never dealt with them in this stock, never." He also swears, "No, sir. I met Mike Porter subsequent, maybe a couple of years later- . . . but I had no dealings with Porter, LeVay concerning Aero Systems" (*Id.*, p. 151). Augus did not testify truthfully.

In Porter's report of PLR's September 1980 activity, he shows that PLR met with "representatives" of Moore

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[91] Porter testified that he had received the Moore Schley report but that he "never read it" and only "realized afterwards this was my report or at least the basis (for it)" (Porter, p. 80, 11. 4-13).

Schley and Mike Porter "[d]iscussed distribution of the Moore & Schley, Cameron report with *Jules Augus. We set up lines of communication for brokers from all over the country to get copies of the report*" (Exh. 991, p. 407-0318) (emphasis added). In October 1980 Porter reported regarding his activities for Aero Systems stock that he "[m]et with Bob Sayegh, Bob Figliozzi and *Jules Augus* . . . (Exh. 994, p. 407 0298) (emphasis added). In January 1981, Porter met with Scheidy and *Augus* and discussed PLR's plans and program for Aero Systems (Exh. 1007, p. 407-0349). PLR's Report for February and March 1981 shows that Scheidy and Figliozzi met with PLR regarding Aero Systems stock (Exh. 1008, p. 407-0378).

They were, as it were, as thick as thieves, and set about to announce the gross misstatements, with the significant omissions, to the public.[92] The impact of the Moore Schley "analysis" was significant as reported to Porter and passed on by Porter to Holmes and Vigman.[93] The Moore Schley report – and its misstatements – were also forseeably picked up and parroted by publications like the Portfolio Letter of September 29, 1980 (Exh. 120).

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[92] Porter reported to Holmes in PLR's October report of September, 1980 activities that PLR had arranged for Augus of Moore Schley to talk to a Dean Witter representative (Exh. 991; p. 407-0324).

[93] Brokers and analysts to whom PLR spoke in September (Exh. 991) reported that they'd read Moore Schley's report (*Id.* pp. 407-0320; 0322; 0325; 0327; 0330); that they found it excellent (0322); that the "company has tremendous upside potential" (0325); that it and the PLR report "awakened up the financial community to the potential in Aero Systems" (0327) and that they "found the company extremely interesting" (0330).

The impact that Holmes, Vigman, PLR, and Moore Schley had on the market for Aero Systems stock is underscored in the testimony of Lawrence Waters ("Waters"), a securities broker for the Investment Corporation of Virginia. Aero Systems first came to Waters' attention in approximately October 1980, when he received a Moore Schley publication featuring the company (Waters, pp. 36-38). Waters described the publication as a "beautiful booklet, pamphlet" (*Id.* pp. 110-111).

Waters spoke with Holmes, who told Waters that several airlines were interested in the CD-3000, and that Aero Systems was "expecting a contract in a couple of weeks" (*Id.*, p. 49). Holmes represented to Waters that with the CD-3000 a major domestic airline, such as Eastern Airlines, could save tens of millions of dollars annually (*Id.*, p. 50). Waters regarded this as an "impressive thing" (*Id.*). Waters remained in contact with Holmes, who continually represented that the contract was always coming "shortly" (*Id.*, p. 72). Waters began to recommend Aero Systems stock to his customers in October 1980 (*Id.*, p. 93), stating that "this thing definitely had the charisma to it. Timing was right, everything was right about it" (*Id.*, p. 96).

Waters did not understand, however, why the CD-3000 never sold since "[Airlift] had tried it, and they had proved beyond a shadow of a doubt, according to what [Holmes] said, that it was definitely a savings of fuel and from that [Aero Systems] expected a contract imminently, and it never came" (*Id.*, p. 74-75).[94] Waters

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[94] See Section 2d below re "Airlift."

testified that Aero Systems' actual earnings were "a disaster" (*Id.*, p. 98), but that "if the CD-3000 clicked the company was on the road to financial stardom. That was the key right there" (*Id.*, p. 101).

Waters stated that without a contract to sell the CD-3000 to an airline, no one should have ever paid more than $5 for Aero Systems stock since "the rest, the five to nine, was the hype" (*Id.*, p. 107-108). From October of 1980 through the end of 1981 most of Waters' clients who purchased Aero Systems stock sold it for a loss (*Id.*, pp. 111-112). Waters attributed the rise in Aero Systems, in part to the activity of firms like Moore Schley (*Id.*, p. 103).[95]

Moore Schley didn't stop with the September 25, 1980 report. Augus issued a follow-up report on November 1, 1980, again restating the false claim that "early testing" showed "fuel savings in the area of 10%" and the false claim of the extent of the market (Exh. 127).

During this time, PLR not only worked hard in step with Moore Schley, but they continued their promotional program of Holmes and Aero Systems. They managed for Holmes to appear in Chicago before a group of brokers in

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[95] Ronald Rotstein, Editor of Capitalgains and an investment advisor (Rotstein pp. 12; 121) concluded from the overall activity in Aero Systems and Aerosonic stocks that there were "certain probabilities that would indicate that there was some type of organized effort in the security . . . " that " . . . the amount of activity suggests to me that there may have been some type of collusionary effort . . . " and that " . . . the activity in these two stocks, particularly . . . Aero Systems, particularly with respect to the volume and price, I thought that that was unusual" (pp. 118; 121).

October 1980 (Exh. 994); they arranged for interviews with Alan Wax, a business reporter for the New York Post, and Paul Stouffer of Investment Dealers' Digest (*Id.*), both of which resulted in articles.

Alan Wax's article appeared in the New York Post[96] on October 13, 1980 and states, once again, that the "unit- . . . can reduce an airplane's fuel consumption by as much as 10 percent" (Exh. 147). This is patently false. Further, Wax attributes to Holmes that "one foreign government already has ordered 250 units . . . " (*Id.*).[97] This is untrue. Porter proudly sent the article to Holmes (Exhs. 986, 994). Wax testified that his article was based on a telephone interview with Holmes (Wax, pp. 30-31), press releases (Wax, p. 28), promotional materials from PLR (Wax, pp. 33-34), and a discussion with Jules Augus of Moore Schley & Cameron Co. (Wax, p. 39). There is no evidence of any correction or retraction by Holmes.

Stouffer's article appeared in The Investment Dealers' Digest in December of 1980 (Exh. 1442). It says "[i]nitial results from business jet users indicate fuel savings to be in the area of 10%. The market for this product includes all multi-engine jet, turbo-prop and piston aircraft in the world." It also omits the same critical information as did Wax's article. Significantly, PLR brought Aero Systems to Stouffer's attention (Stouffer, p. 18).

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[96] At the time that this article was written, the New York Post had a circulation rate between 600,000 and 900,000 papers daily (Wax, p. 22).

[97] Holmes admits that as of November 1980, Aero Systems had not received orders for 250 CD-3000's from any source or aggregate of sources (RFA's 221-225).

When Stouffer called Aero Systems, "Holmes insisted on doing all of the speaking himself" (Stouffer, p. 19), and told Stouffer that "the exciting new product [CD-3000], has all the potential . . . to become the major portion of the firm's business, far outdistancing its present products" (Stouffer, p. 38).

All of the sudden interest in Aero Systems stock was compounded by another Aero Systems marketmaker, Wheat First Securities, issuing a stock report on Aero Systems on November 6, 1980 (Lind, pp. 10-11; Exh. 5767). Again, Wheat First states that "initial results from business jet users indicate fuel savings as high as 10% . . . " and that the "market potential . . . includes 5,500 units for commercial airlines, 50,000 for multi-engine general aviation aircraft, 8,500 for helicopters[98] and an extremely large military market." Lind's experience virtually mirrors Stouffer's contacts with Aero Systems. Moore Schley promoted Lind's interest in Aero Systems (Lind, p. 15), and Lind reviewed materials Moore Schley prepared on Aero Systems (Lind, pp. 26-28). Lind met with Holmes at Aero Systems in Miami in preparation of the November 6, 1980 article (Lind, p. 34).

Lind described Aero Systems as "a company that had a technology angle in it, or there was a technology play

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[98] This is a falsehood. Helicopters have absolutely no use for such a "fuel savings" device. For all helicopters, maximum specific range occurs at the limit speed of the aircraft. Therefore, to maximize specific range, the pilot simply flies the helicopter as fast as it will go (Davies, pp. 54-57). Holmes admitted that the CD-3000 was never tested in a helicopter (Holmes, p. 279).

within it in the company" (Lind, p. 21). Lind viewed Aero Systems as "a base business, but with a potential technology lever" (*Id.*). That lever was the CD-3000, and that without "the potential rewards that could be generated from the CD-3000," Lind would not have written the article (Lind, pp. 22-23). Holmes saw the report and, despite the misrepresentations and omissions, did not correct or attempt to retract it (Holmes, p. 279).

Further, the November 1980 Investment Alert carried the same basic story with the same omission (Exh. 130). However, it categorically states that "[t]his system *can* effect fuel savings up to 10%" (emphasis added).

On January 5, 1981 Mike Pollick and the Orlando Sentinel Star reported that Aero Systems concluded that the U.S. market for the device includes 6000 commercial planes and 50,000 general aviation planes. He also notes that the "company's own projections indicate very rapid growth in sales and earnings" (Exh. 5223).

Holmes then sent out a shareholder letter on January 12, 1981 (Holmes, p. 361; Exh. 5224). He states that "several airlines are on the verge of placing orders . . . and we have many pending orders from the business aircraft market." These statements are false; Holmes knew that *no* airlines were on the "verge" of buying the device. Further, there were *not* "many pending orders" for business jets. In fact, there were only *two* orders for the device "pending" at the time of Holmes' shareholder letter; one each to Associated Radio, Co. and Arkansas Modification Center (Exh. 5284).

Holmes' shareholder letter is also significant in that, for the *first* time in *10 months* since Holmes signed the

agreement, Holmes stated he's *starting* to advertise the device to the *aircraft* market – rather than advertise the device to his *stock* market.

Of course, Moore Schley trumpeted the same false "facts" in its memo of January 12, 1981 to its customers and brokers (Exh. 133). Moore Schley added that they were "confident that results will be substantially greater . . . sparked by expected orders for the CD 3000 . . . " (*Id.*).

Holmes further fueled the fire by appearing on "The Nightly Business Report" (Channel 2, Miami) on February 4, 1981 with reporter Eugene Teibloom (Teibloom, pp. 30-32; Exhibit 5228). Holmes requested the videotape of the appearance and distributed it widely (Holmes, pp. 833-836). The text repeats that the device "reportedly produces fuel savings of 10 percent on private planes . . . " Moreover, in the release, Holmes made a new misrepresentation that *commercial airlines* using the device can produce "an estimated 4 to 10 percent" savings for which there is absolutely no foundation (Exh. 5228).[99]

Finally, the totality of the release regarding the Teibloom interview clearly implies that Eastern Airlines

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[99] It was only eight days before, on January 27, 1981, that Holmes signed an agreement with Airlift International, Inc., described as a "commercial airline", to *provide* Aero Systems with "documented fuel saving operating results" (Exh. 5226); none whatsoever existed at the time of the Teibloom show (Sovacool, p. 69). Also, this is the first indication to the public that Holmes and Aero Systems are finally trying to sell the device to an airline, the very target Holmes saw for the device nearly a year earlier.

would buy the CD-3000 and that the device would save 5% of fuel costs amounting to $50 million dollars in 1981.

The misrepresentations concerning fuel savings continued. In March 1981, in the ABD, Aero Systems placed an ad claiming "up to 10% fuel conservation" (Exh. 5234). Smart Money published an article in its April 1981 issue stating that "[w]ith the CD-3000 a pilot can save from 4% to 16% (of fuel) . . . " (Exh. 137). Also, in an article appearing in the OTC Review in July 1981, it's again reported that the CD-3000 " . . . is designed to reduce an airplane's fuel consumption by as much as 16 percent . . . " (Exh. 5244A). On June 17, 1981 Holmes released over PR Newswire that "The CD-3000 . . . *can* save up to 10% of the fuel consumption . . . " (Holmes, pp. 500-501; Exh. 5242) (emphasis added).

d. Holmes Released Faise and Misleading Information Regarding Airlift International

On January 27, 1981 Holmes issued a press release stating that Aero Systems had signed an agreement with Airlift International, Inc. ("Airlift"), describing Airlift as the "first commercial airline user" of the CD-3000 (Exh. 5226). Holmes claims that "Airlift will also provide Aero with documented fuel savings operating results" (*Id.*). This announcement appeared in Barron's on February 2, 1981 (Exh. 5227), the February 9, 1981 Aviation Week publication (Exh. 5232), and Fortune Magazine on March 9, 1981 (Exh. 5235).

Holmes failed to disclose that all Airlift flew as a "commercial" airline were freighters (Sovacool, p. 57) and that the CD-3000 was going to be "tested" on Airlift's

long distance airplane (Sovacool, pp. 57-58). He did not disclose that such "tests" on a single aircraft vary not only with respect to the types of aircraft involved but aircraft within the type itself (Sovacool, pp. 123-124). He failed to disclose that loss of time caused by use of the CD-3000, a serious concern of passenger airlines, was of no concern to Airlift (Sovacool, p. 164). He failed to disclose that slowing cruise time[100] of an airline aircraft increases crew and maintenance costs, and that as incremental costs approach the marginal cost of fuel, the value of the CD-3000 diminishes (none of which was considered by Airlift or in its report) (Sovacool, pp. 130-131). Finally, he failed to disclose that the pilot can obtain the same results by using a flight plan as from using the CD-3000; the CD-3000 only makes the information more convenient (Sovacool, pp. 82-83).

Holmes then sent a letter to shareholders on March 16, 1981 telling them that Aero Systems is "currently installing [the] CD-3000 . . . on our first large commercial jetliner" (Holmes, p. 383; Exh. 1011). He makes the same omissions, and additionally, chooses not to name Airlift International. He finally acknowledges that "pilot acceptance is the key" to the success of the device (*Id.*), one of the cautions told to him by Hayden a year before.[101]

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[100] Cruise time is the time that you enter into a steady state operation from the top of the climb until the top of the descent (Sovacool, pp. 128-129).

[101] The prospect of "real" test data from Airlift International also coincided with Holmes' discharge of PLR on April 20, 1980 (Exh. 1009). It's submitted that Holmes didn't need PLR's further assistance or costs in disseminating Holmes' phoney statistics.

Holmes continues to emphasize that the company is "on the verge" of success; *i.e.*, " : . . . [t]he documented results are expected to be the trigger to volume sales and leases to the world's major airlines. We are now more confident than ever about the success of our CD-3000 . . . and feel we are on the verge of a major breakthrough" (*Id.*).

On May 7, 1981 Holmes issued another press release (Exh. 1038).[102] Holmes reveals that "preliminary indications" of the testing by Airlift "appear to be quite significant" (*Id.*). He "quotes" Sovacool to the effect that he, Sovacool, has recommended that Airlift "outfit the entire fleet" with CD 3000's.[103] The letter further states that the tests have not been completed, and Holmes says the tests are scheduled to "continue for another week . . . " after which the data must be "consolidated and compared with prior fuel consumption . . . in order to document . . . fuel savings." The alleged test data on which the *final* report was based was already completed by this date; the final report shows the "testing" took place between March 15 and April 15, 1981 (Sovacool, p. 120; Exh. 1039). Thus,

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[102] On May 1, 1981 – six days before this first public release which in any way relates to any actual testing, or whether or not the tests were "encouraging," Moore Schley distributed a report to its brokers stating that Airlift test results are "quite encouraging" and that "[f]inal [test] results should be available shortly" (Exh. 139). That was not public knowledge on May 1. Regardless of whether or not the statements were true, it appears that Holmes passed on inside information which was used by Moore Schley.

[103] The fact that the "entire fleet" consisted of a total of nine planes (Sovacool, p. 58) was not disclosed. Also, the "quote" by Sovacool was written by Holmes, not Sovacool. (Holmes, p. 1907).

Holmes misrepresented the extensiveness of the testing, and that it was to continue.[104]

In another letter to shareholders on May 18, 1981, Holmes repeats Sovacool's "quote" and states that Sovacool says the device "does more than [was] anticipated" (Holmes, p. 486; Exh. 145). In fact, Sovacool testified that he had no way to anticipate any particular percentage of fuel savings (Sovacool, p. 32).

The Airlift International report was released on July 14, 1981 and was signed by Robert Sovacool, Airlift's Director of Flight Operations (Exh. 1039). Holmes drafted both Sovacool's forwarding letter and the report, and Sovacool signed them (Holmes, pp. 1911-1912; 1914). Holmes can't point out any changes made by Sovacool (Holmes, p. 1915). Holmes had first received the report in June (Holmes, p. 1911). This report, which Holmes calls the "Airlift test package" (Holmes, p. 1913) was the report which Holmes sent to other airlines (Holmes, pp. 1912-1913).

On July 24, 1981 Holmes sent *another* letter to shareholders extolling the Airlift test results (Holmes, p. 517;

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[104] Neither Aero Systems nor Holmes have produced any "test" results, raw data, calculations, compilations, analyses or other documents to back up the Airlift "tests". Sovacool says they were given to Aero Systems (Sovacool, pp. 83-84; 87; 104-105). The documents Sovacool says were given to Aero Systems were not produced by Aero Systems in this litigation despite repeated efforts to get them (Taylor Decl. ¶6). The fact that documents of such obvious importance to Holmes were not produced raises serious questions not only as to the validity of any interpretation of their results, but of their very existence.

Exh. 149). He states that "even though Airlift temporarily ceased operations prior to collecting sufficient data . . . their best estimate is that the final results . . . could reflect fuel savings in excess of 10% . . . " Holmes does not tell his shareholders that Airlift went bankrupt in June, 1981 (Sovacool, p. 8), that after bankruptcy was filed, the aircraft (with the CD-3000 on it) was repossessed and when Airlift got it back, the CD-3000 was gone (Sovacool, p. 39). Holmes says that the tests are "expected to generate immediate sales" to operators of DC-8-63's (Airlift's type of craft).[105]

Further, the Airlift report itself, approved by Sovacool but written by Aero Systems (Sovacool, p. 115; Exh. 1039),[106] Holmes admits writing most of the report (Holmes, p. 1906).

The report clearly states that 2% of the alleged fuel savings is speculative because tests "were interrupted" before comparative calculations could be made (Exh. 1039, p. 001 01592) and that the total resulting savings would be "*between* 4% and 6%" (*Id.*) (emphasis added),

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[105] Note that several DC-8-63 operators were unable to use the CD-3000 to achieve maximum specific range, because instability resulted, forcing the pilot to burn additional fuel to regain stable cruise conditions. (*See, e.g.*, Exh. 3884). Further, by December, 1987, only one CD-3000 was sold to be installed in a DC-8-63 (Exh. 5284).

[106] Holmes admits that the Airlift report itself was *not* sent to shareholders (Holmes, p. 1966).

not that they would be "in excess of 6%" as he later tells his shareholders.[107]

Against this storm of hyperbole and unsupported representations by Holmes of the "fuel percentage savings" to his shareholders and the stock buying public, one must measure what Aero Systems *really* believed the CD-3000 could do.

On July 1, 1981 George Nelson, the recently hired Vice-President, Fuel Computer Marketing, who had the primary responsibility for the world-wide marketing of the CD-3000 (Exh. 5242), sent letters to Japan Air Lines, Gulf Air, Dan Air Service, Cathay Pacific Airways, All Nippon Airways, Air France, Muse Air, Deutsche Lufthansa, Sudan Airways, Transavia Holland and UTA guaranteeing *only* 2% fuel savings by use of the device (Exhs. 3848). Thus, what Holmes was telling the stock-buying public and what Aero Systems was telling those who were sophisticated in the business were two entirely different things.

4. An Aero Systems Corporate Officer Resigned Because of the Press Releases.

The effect of what Holmes and Vigman were putting out was not only felt by the public. George Jackson, with

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[107] Holmes' obsession with "percentage of fuel savings" is not to be underestimated. According to this [sic] own representations of the size of the market – 30 billion dollars – a one percent reduction in fuel costs, equals 300 million dollars! Thus, a misrepresentation of only 1% to his shareholders and the public is not a *de minimus* representation.

the company since March of 1978, and Secretary and Controller of Aero Systems, who reported to Holmes (Jackson, pp. 6-7), resigned on September 26, 1980 (Exh. 1) because of what was going on.

Holmes was the one in the company who made contacts with Aero Systems marketmakers (Jackson, p. 7). Holmes prepared and issued press releases (*Id.*, p. 15). Shortly after the CD-3000 was acquired, the flavor of the press releases changed from the prior years he was there (*Id.*, p. 18). They became overly optimistic (*Id.*, and p. 29). Jackson became concerned about the press releases and projections by Holmes (*Id.*, pp. 14-15; 17).

Jackson became so concerned that he consulted Aero Systems' SEC counsel (*Id.*, p. 14). Jackson told the SEC attorney that Holmes had "gone off the deep end" and that Aero Systems was a "paranoid company" (*Id.*, pp. 29; 31; Taylor Decl. ¶5). The company counsel also expressed concern about the press releases (*Id.*, p. 15).

Jackson then, without Holmes' knowledge (*Id.*, p. 20), consulted independent SEC counsel (*Id.*). They told Jackson that he "could go along with what's happening and ignore it, or . . . resign . . . " (*Id.*). He resigned (*Id.*, p. 21) because his concerns were so great he felt he had to remove himself from the source of the problems (*Id.*, p. 26).

Jackson was "nervous that the stock was going up and it was all, I thought, from the press releases . . . " (*Id.*, p. 23) "directly related to the fuel management computer" (*Id.*, pp. 36-37). The press releases were tied in with the stock and he was nervous about those press releases going to the public (*Id.*, p. 48). "The stock rose

fairly rapidly in a short period of time. . . . (Aero Systems') earnings weren't there to support that kind of rise and in (Jackson's) opinion it was all based upon the press releases issued regarding the potential future profits of the fuel management computer, not on current profits" (*Id.*, pp. 41-50). The Aero Systems "stock price was not justified by the earnings" (*Id.*, p. 48). Although he wouldn't admit in his deposition that he had said it, Jackson considered the CD-3000 "a gimmick" (Taylor Decl. ¶5).

Jackson did discuss his concerns and the press releases with Holmes "a couple of times" (*Id.*, p. 44) but felt he wasn't "going to be strong enough to influence him in these matters and that's why I sought individual counsel" (*Id.*, p. 25).

L. HOLMES PARTICIPATED IN AND ASSISTED IN THE BUNNINGTON STOCK MANIPULATION

Holmes was a direct participant of the Bunnington stock manipulation, and aided and abetted that manipulation.[108] It was done by Holmes through Lugo and Moore Schley, both of which had so greatly benefited Holmes and Aero Systems.

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[108] It is the opinion of John Torkelsen, one of plaintiffs' experts, that the stock of Bunnington was manipulated (Torkelsen Decl. ¶22).

1. Holmes Invested Heavily in Bunnington Through Private Transactions

Aside from the transactions between Holmes and Bunnington set forth above, and his relationship with the Bunnington principals, Holmes was familiar with Bunnington and was a substantial shareholder of Bunnington.[109] Holmes received Bunnington Annual Reports and shareholder letters (Holmes, p. 996).

As set forth above, Bunnington was formed in 1969 and a portion of its stock was distributed to public shareholders of Corporate Enterprises through a "spin-off."

In addition to the Bunnington stock Holmes received by virtue of Holmes' ownership of Corporate Enterprises, Holmes purchased 20,000 shares of Bunnington stock through a private placement in 1969. The purchase price for the 20,000 shares was $50,000 (Exh. 3986).

In September of 1979, Holmes purchased a convertible debenture from Bunnington for $100,000 (Holmes, p. 2880, Exh. 3989). The debenture was convertible into 40,000 shares of the common stock of Bunnington

[109] Holmes also was familiar with Aerosonic. In January, 1980 Ronald Rotstein of Capitalgains spoke with Holmes (Exh. 2631). Rotstein asked Holmes about Aerosonic (Rotstein pp. 46-47). Holmes told Rotstein that Holmes "[k]nows Aerosonics-recording altimeters used in conjunction with collision avoidance systems (CAS) *have the capability to drastically reduce air crashes*" (emphasis added), but told Rotstein "no direct quote here" (Rotstein, pp. 46-47). It is this "CAS" device – again a gimmick that could *not* "drastically reduce air crashes" as Holmes misrepresents – that Aerosonic was hyping to push its stock price up.

(Holmes, p. 994). Holmes converted the debenture to stock in July of 1981, just prior to the collapse of the market price for Bunnington stock (Exh. 3863).[110]

Holmes asserts that he purchased additional stock of Bunnington on October 20, 1980 through a private placement (Holmes, pp. 2864-2865; 2046-2047; Exhs. 3863, 3987). The sale actually took place on November 11, 1980 (Exh. 3987). Holmes paid $150,000 to acquire the 50,000 shares of Bunnington (at $3.00 per share) (Holmes, p. 2864-2865, Exhs. 3863, 3987). On the following two days, Holmes sold 50,000 shares of Aero Systems stock through Moore Schley, more than enough to pay for the Bunnington securities (Exh. 3863).[111]

[110] This clearly provides a strong motive for Holmes to assist in the Bunnington manipulation. Holmes' cost basis was $2.50 per share; at the time he converted, Bunnington's price was 10 5/8 per share (Foley Decl. ¶¶91-92). The two year waiting period under Rule 144 was to expire in September 1981. Holmes only missed by two months.

[111] Holmes' 144 sale of 50,000 shares of Aero Systems stock through Moore Schley on November 11 and 12, 1980 (Exh. 3863), not only made Holmes a whopping profit, and provided money to fuel the Bunnington manipulation, but also represents Holmes' reward to Moore Schley for a job well done. As Sayegh of Moore Schley testified "[a]ny trading firm on Wall Street obviously tries to get the flow of stock . . . There is a constant competition amongst all firms to get the buyers and the sellers" (Sayegh, p. 68). When Holmes initially decided to sell 50,000 Aero Systems shares, he was going to sell 25,000 to Moore Schley and 25,000 to Wheat First (Holmes, p. 967, ll. 12-15; Exh. 171). But Holmes "changed his mind" and directed that all 50,000 shares were to be sold to Moore Schley (Holmes, p. 967; Exh. 172).

2. Holmes Actively Traded Bunnington

In addition to Holmes' purchase of Bunnington stock and the debenture through private transactions, Holmes traded heavily in Bunnington stock to assist Lugo and Bunnington in the manipulation of Bunnington stock.

During the period of time from September 3, 1977 through May 20, 1981, Holmes purchased 61,900 shares of Bunnington on the open market. The aggregate cost of the purchase was $364,875.00 at an average cost of $5.79 per share. A total of 60,900 of the shares purchased were subsequently sold for total proceeds of $357,203.57, at an average price of $5.87 per share (Foley Decl. ¶ 90).

Holmes purchased 45,900 of the Bunnington shares through FSSC in twelve transactions (Foley Decl. ¶ 93). Holmes received preferential treatment from FSSC in connection with his purchases, at prices lower than the lowest NASDAQ reported asking price. This preferential pricing amounted to a total of $13,237.50 to Holmes' benefit (Foley Decl. ¶ 94). With the exception of one transaction, these securities were sold through broker-dealers other than FSSC in sixty-six separate transactions (Foley Decl. ¶ 95). This created the appearance of market activity, which had the natural result of artificially maintaining or raising the market price of the stock (*See* Foley Decl. ¶ 103).

Holmes' purchases assisted Lugo in creating market demand for the securities and controlling the public float of Bunnington stock (Foley Decl. ¶ 99). Nine out of twelve of Holmes' purchases between May 31, 1979 and May 20, 1981 represented more than 51% of NASDAQ's average daily volume (Foley Decl. ¶ 98). Further, between

March 1, 1981 and July 24, 1981, Holmes was the largest buyer of Bunnington stock from FSSC, for 10,000 shares (Foley Decl. ¶ 99). This occurred at a time when there was no active market for Bunnington stock (Foley Decl. ¶ 102).[112] During the same period, the largest seller of Bunnington stock was Vigman, selling 17,000 shares under Rule 144. (Foley Decl. ¶ 100)

Holmes' profit from these transactions amounted to only $363.48. It is a triable issue of fact whether or not purchases at FSSC and subsequent sales were made for the purpose of assisting Lugo with the domination and control of the float of Bunnington common stock (Foley Decl. ¶¶ 98, 99, 124).

3. Holmes Actively Promoted Bunnington

Holmes tried to involve Porter, LeVay & Rose with Bunnington. Holmes asked Porter to represent Bunnington and asked PLR to send its materials to Bunnington (Porter, p. 49, ll. 9-15). Porter, wisely, decided against it (Porter, p. 49, ll. 18-19).

Holmes also promoted Bunnington to Herb Sheidy, the analyst with Moore Schley (Sheidy, pp. 128-129). Holmes asked Sheidy if Moore Schley would be interested in looking at Bunnington with a view toward making a recommendation of Bunnington stock to their customers or making a market in the stock (Sheidy, pp.

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[112] During the March 1 through July 24, 1981 period, a total of 145,000 shares of Bunnington were sold by FSSC customers. Only 47,000 shares were purchased (Foley Dec. ¶¶ 99, 100).

129; 144).[113] Holmes recommended that Moore Schley make a market in Bunnington (Holmes, p. 983). Holmes told Moore Schley about Universal Silicon[114] and its connection with Bunnington (Holmes, p. 991).[115]

On May 6, 1981, Bunnington issued an announcement of its acquisition of Universal Silicon (Exh. 1683). In the release, Bunnington touted the "anticipated" success of the new subsidiary's polychrystaline silicon process.[116]

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[113] Bunnington only had 6 market makers in may [sic] – June, 1980 (Foley Decl. ¶ 135). There was little market activity in Bunnington stock at that time (Foley Decl. ¶¶ 102, 103). Holmes was attempting to create a market in Bunnington for two reasons: to protect his own economic interest and to protect that of his friends at Bunnington. Who better should Holmes attempt to entice but Moore Schley which had done so well by him in the past.

[114] Holmes also discussed Universal Silicon with Vigman (Holmes, p. 993).

[115] Universal Silicon was supposed to develop low cost "electronic grade" silicon, a material used in computer chips and transistors (McNeil, pp. 873-875). This is another in the long line of "products" that were guaranteed to draw the attention of the stock-buying public; another "gimmick." Universal Silicon predictably failed and by January 1986, the operation was shut down (McNeil, p. 875-876).

[116] Bunnington prepared a release on May 5, 1981 which was identical to the May 6, 1981 release (Exh. 1682). McNeil testified that he couldn't recall the reason for the duplication, but that he didn't believe Bunnington had sent out two identical releases, and that it was not a draft of the May 6, release (McNeil, pp. 891-893). However, since Holmes bought 5,000 shares of Bunnington on May 5, 1981 it is a reasonable inference that he either did so with insider information or did so as

(Continued on following page)

Holmes telefaxed Sheidy of Moore Schley a copy of the May 6, 1981 Bunnington press release to help create interest in Bunnington (Sheidy, pp. 132-134; Holmes, pp. 996-998; Exh. 187).

The May 6, 1981 press release was false and misleading. It failed to disclose: (a) that the commercialization of polychrystaline silicon was a "high risk" venture; (b) that Bunnington lacked the capital to fund Universal Silicon so a partnership including Vigman, Diamond and McNeil was established to infuse capital; and (c) that the polychristaline silicon process was subject to potential claims by Aero Chem, claims that later resulted in a lawsuit over the rights to the process (McNeil, p. 868; Exh. 6739; Gould, pp. 8-12; 42, 43).

Following receipt of the Bunnington press release Holmes continued to actively promote Bunnington to Moore Schley. Sheidy and Holmes had other discussions regarding Bunnington, and Holmes requested that Moore Schley look at Bunnington (Sheidy, pp. 141-142). Figliozzi also had conversations with Holmes regarding Bunnington (Figliozzi, p. 324-325). Further, Sheidy, Figliozzi, Augus and Sayegh (all of Moore Schley) had dinner with Holmes and McNeil in New York (Sayegh, p. 54).

Holmes again spoke with Sheidy on June 19, 1981 regarding Bunnington and its acquisition of Universal

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a result of an agreement with his friends to delay the release so he could purchase before the release had its desired effect. The price of Bunnington rose from 11 1/4 bid on May 5, 1981 to 11 7/8 bid on May 7, 1981 (Foley Decl. ¶ 136).

Silicon. During the conversation Holmes provided Sheidy with additional information concerning the silicon operation and related to Sheidy information concerning the availability of funds from Monsanto Corporation which might have an impact on Bunnington's prospects (Sheidy, pp. 143; 147; Exh. 183).

Holmes' interest in promoting Bunnington stock appears to be related to his relationship with Vigman, Diamond and McNeil rather than an interest in the company's product. Holmes testified that he liked the people at Bunnington and liked the fact that Vigman was associated with them. (Holmes, p. 984).

M. HOLMES' EFFORTS TO SUPPORT THE PRICE OF BUNNINGTON STOCK AFTER THE COLLAPSE IS EVIDENCE OF HOLMES' PARTICIPATION IN THE SCHEME

On July 21, 1981, FSSC and Sebag ceased making a market in the Bunnington stock, due to their capital deficiencies. The closing market price for Bunnington was 10 3/8 bid/10 5/8 ask on July 20, 1981. The market price of Bunnington had dropped to 3 bid/3 1/2 ask by July 27, 1981 (*Id.*).

Holmes again stepped into the breach and "paid" his friend Vigman. He made a substantial effort to prop up his friends' company, and maintain the price of Bunnington's stock.

Holmes purchased 48,000 shares of Bunnington through Moore Schley on July 28 and 29, 1981 (Exh. 3863, 1. 107, 108). Further, during the period between July 28, 1981 and November 13, 1981 Holmes purchased 172,137

shares of Bunnington stock on the dates and at the prices indicated at ¶¶ 115-117 of Foley's Declaration. This was a continuing effort by Holmes to maintain Bunnington's stock price (Foley Decl. ¶ 119).

Further, in order to be able to invest so heavily, Holmes *borrowed* $600,000, secured by 528,000 shares of Holmes' Aero Systems stock, specifically to acquire Bunnington stock and to retire a $100,000 loan at the bank (Holmes, pp. 1031-1034; 3199; Exhs. 5279, 5280).

Finally, Holmes believed that a public company should have the broadest stockholder base possible (Holmes, pp. 2614, 2618). In a transaction that defied the logic of at least one broker,[117] in July 1983, Holmes caused Aero Systems to distribute Bunnington stock which he had sold to Aero Systems shareholders (Holmes, p. 2763; Exh. 3968) which numbered over twelve thousand (Exh. 3968). By his acts, he again "paid" his friends at Bunnington by enlarging Bunnington's shareholder list to at least the number of Aero Systems shareholders.

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[117] Lawrence Waters, Vice President and retail broker at the Investment Corporation of Virginia, spoke to Holmes after the release of Aero Systems' 1983 Annual Report. (Waters, p. 64; Exh. 5261) Waters noticed Holmes "owned a big position in Bunnington." Waters "asked [Holmes] what type of stocks had he bought. And he said he had just bought 150,000 shares of Bunnington and it was a good one to own" (Waters, pp. 64-65). Waters followed Bunnington stock for a year but, "it never moved, never, it didn't move an eighth. In fact, it went down . . . Maybe a year or so later . . . all of a sudden it started to pick up steam" (Waters, p. 123). Bunnington climbed to around

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N. HOLMES PARKED BUNNINGTON STOCK WITH LUGO

On May 18, 1981, FSSC's inventory reached an all time high of $688,378. Included in FSSC's inventory were 19,208 shares of Bunnington common stock with a market value of $235,298. At this level of inventory, FSSC's Net Capital was deficient by $136,222 (Foley Decl. ¶ 46).

In May of 1981, all trades through May 21st were included in FSSC's net capital computation for its monthly Net Capital Report to the NASD (Foley Decl. ¶ 52).[118]

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six dollars a share (Waters, p. 118). When Holmes told Waters that Aero Systems was going to pay a dividend of Bunnington stock, Waters said "that knocked me for a loop . . . you're giving us a piece of nothing thats going to cost people more to sell it than its worth. And he said, "well, we've decided that's what we're going to do" (Waters, pp. 117-118); "He seemed to be giving it away, flat giving his stock away" (Waters, p. 134). At the time Aero Systems paid the dividend of Bunnington, the Bunnington stock was selling at six dollars a share (Waters p. 118). Waters testified that [Holmes] had a three point profit. "He had a four hundred thousand dollar profit. He just could have sold it on the open market, and he was giving it to the shareholders at three, but at what benefit, if he wasn't receiving any cash from it? And I couldn't figure out why he was giving it away" (Waters p. 135).

[118] FSSC reported its Net Capital to the NASD on a monthly basis, using the last Friday settlement as the closing date for financial statement and net capital computation. Trades as of May 21st were [sic] be settled on May 29th, allowing five business days and one extra day to allow for the Memorial Day holiday, pursuant to the NASD Uniform Practice Code Paragraph 3504, Section 4 (Foley Decl. ¶ 52).

In order to create the appearance of compliance with the Uniform Capital Requirements under SEC Rule 15C-3-1, Lugo "parked" securities with customers to conceal the true state of its inventory positions from the NASD (Foley Decl. ¶¶ 47, 51).

Holmes' account at FSSC was one of the customer accounts used for parking securities that were properly attributable to FSSC's inventory. On May 20, 1981, an order to purchase 5,000 shares of Bunnington stock was entered in Holmes' account. The transaction reflected a purchase price of $61,250.00, with payment to be made by delivery to Holmes' bank, First Southeast National Bank of Miami Springs, Florida (Foley Decl. ¶¶ 49, 55, 63).

The transaction reduced the value of the Bunnington inventory by $61,250, thereby reducing the amount of capital required by the SEC. However, this was not a *bona fide* transaction (Foley Decl. ¶ 51, 58).

On May 29, 1981, an order to sell 5,000 shares of Bunnington was entered in Holmes cash account at FSSC, for a sale price of $61,875 to be settled on June 5, 1981 (Foley Decl. ¶¶ 53, 54).

On June 1, 1981, four days before settlement of the May 29 sale of the 5,000 Bunnington shares, FSSC made a prepayment of $61,875 to Holmes. This occurred prior to Holmes' payment for the purchase of the securities on May 20, 1981 (Foley Decl. ¶ 53, 54).

To make the prepayment on June 1, 1981, FSSC had to borrow funds from SCCP. An employee of FSSC, Robert Reber, delivered the check which Holmes endorsed over to his bank. On the same day, Holmes' bank wired

$61,250 to SCCP to be credited to the FSSC loan account for payment of the stock originally purchased on May 20, 1981. Ordinarily, payment would be made by a draft sent to FSSC's own bank to be credited to FSSC's bank account (Foley Decl. ¶¶ 53, 54).

Through these transactions, Holmes "paid" for the 5,000 Bunnington shares with the FSSC's funds. This is known as a "free ride", and is expressly forbidden by a SEC Rule. Further, FSSC's inventory of Bunnington stock was increased by 5,000 at a value of $61,875 (Foley Decl. ¶¶ 61, 62).

The shares sold on May 29, 1981 (settling on June 5, 1981) appear to be the same ones purchased on May 20, 1981, although Holmes claims that they are not (Holmes, p. 2842). Holmes claims that the shares sold on May 29, 1981 were purchased on May 5, 1981 through Lugo in Holmes' DVP account at FSSC, and claims that they were delivered to cover the May 29, 1981 sale (*Id.*).

However, it does not matter which certificates Holmes delivered to cover the May 1, 1981 sale, since even if the certificates for the May 5 purchase were delivered, it still does not change the effect that the May 20, 1981 purchase had to mask FSSC's net capital deficiency. The transaction was a park, particularly because the sale takes place soon after the May net capital reporting period, and because the proceeds from the May 29, 1981 sale (paid in advance) were used to pay for the May 21 purchase (Foley Decl. ¶ 58, 61, 62).

The following chronology of the sale and prepayment on June 1, 1981 shows the coordination between Lugo

and Holmes to execute the "parking" transaction, while maintaining the appearance of legitimacy:

a. Holmes endorsed the check;

b. Reber hand delivered the check to Holmes' bank on June 1 for deposit;

c. The bank stamped the check and sent it through the clearing house on June 1;

d. The bank wired to SCCP the $61,250 needed to pay for the DVP purchase on June 1 to credit the FSSC loan account;

e. FSSC borrowed $125,000 on June 1 to cover the check to Holmes;

f. Holmes paid for the stock purchase after he received the prepayment, in effect, using FSSC's own funds to pay for the purchase;

g. Holmes sold 53,900 shares on 64 different trades between March 2, 1979 and June 16, 1981. The 5,000 Bunnington share sale on May 29, 1981 was Holmes' only sale through FSSC during the March 2, 1979 to June 16, 1981 period (Foley Decl. ¶ 57, 63).

O. HOLMES AND AERO SYSTEMS PARTICIPATED IN DASH STOCK MANIPULATION THROUGH THE CASCADE DATA DEALERSHIP AGREEMENT

Holmes' involvement with Blumenthal stretches back to the days of J. C. Roberts. Blumenthal was also a shareholder in DCS Financial, and received shares of Aero Systems stock when DCS merged with Aero Systems Avionics.

In 1977, Blumenthal joined with Dash Industries, Inc. (Exh. 4881), a Miami-based manufacturer of wall coverings and draperies (Blumenthal, p. 320). Dash Industries, until that time, had been controlled by Philip Dash, and his son, Jay Dash (Exh. 4882).

In 1980, Blumenthal was introduced to Robert McAndrews, president of Cascade Data, a computer manufacturer doing business in Michigan. Blumenthal and Robert McAndrews ("McAndrews"), Cascade's president, agreed that Cascade would merge with Dash, and receive a cash payment of $400,000.00 and, additionally, McAndrews was to receive 925,000 shares of Dash common stock (Dash RFA 54). Subsequently, McAndrews learned that Blumenthal wanted to have access to "a team of stockbroker marketers" . . . "until the insiders [could] sell enough stock." (Exh. 2952; McAndrews, pp. 57-64, 4/16/88)

FSSC was a market-maker in Dash stock (Lugo, p. 440; Blumenthal, pp. 407-408). Like Aero Systems, the price of Dash stock rose based upon false and misleading press releases. In Dash's case, the press releases, later repeated in various news articles, contained false financial information (Exhs. 515; 414; 4890; 4893; 643; 639) and information about computer products which were either misrepresented or didn't exist at all (Exhs. 494; 4918; 638; 645 and 515; Koscic, pp. 78-80; 84-89).[119]

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[119] For example, C. Stephen Carr (Mr. Carr is a computer expert; his qualifications are found at pp. 9-19 of his deposition.) testified that Dash published misleading information about the identity of Cascade's competitors (Carr, p. 128), Cascade's marketing plan (*Id.*, pp. 131-132), and that Cascade was a designer and manufacturer of main frame computers (*Id.*, p. 56).

One element in Dash's scheme to manipulate the price of its stock was a public relations campaign regarding the number of retail outlets that would sell Cascade Data computers. Repeatedly, Dash publicly stated that Cascade Data would have 1,000 retail outlets for its product (Exh. 4918).[120]

In 1980, Bob Holmes of Aero Systems met with Blumenthal and McAndrews (Blumenthal, pp. 263). As a result of their meeting on October 16, 1980, Aero Systems, an airplane parts business, became a retail computer outlet for Cascade Data and Dash Industries (Ashton, pp. 247-248; RFA 923). Dash seized the opporutnity to hype its growing network of computer dealers (Exh. 1407).

Less than eight months later, on June 12, 1981, Aero Systems cancelled the dealership agreement with Cascade Data stating, among other things, that Cascade computer components were so common in the computer industry that Aero Systems could build it themselves (Ashton, p. 248; RFA's 927, 928, 930).

Aero Systems' "dealership" purchased only one computer, and had no sales (Exh. 3313). These facts result in a compelling inference that the only purpose for the Aero Systems dealership was to create public exposure and initial media coverage for both Dash and Aero Systems.

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[120] Carr analyzed the business and operations of Cascade Data and opined that, given the company's capitalization, it was virtually impossible for Cascade Data to establish 1,000 retail outlets for its product (Carr, p. 122).

P. THE EFFECT OF THE MANIPULATIVE SCHEME ON THE CAPITAL OF FSSC AND SEBAG

1. FSSC – March 1981 to July 1981

At the end of March 1981, FSSC had a capital deficiency. Although FSSC had net capital in excess of $67,841 – there was a deficiency of $120,273 in the Customer Reserve Account. Since there was only $16,000 in the FSSC checking account, Lugo should have either sold inventory to raise cash to meet the requirement or obtained a major infusion of capital from FSSC's principals. Lugo did neither (Foley Decl. ¶¶ 32, 33).

Between March 27, 1981 and April 24, 1981, FSSC's inventory value more than doubled, from $182,000 to $415,000. During this time, FSSC's capital declined 40% for a net capital deficiency of $16,625, and FSSC's Customer Reserve Account deficiency grew to $199,793. (Foley Decl. ¶ 32-34).

During this time period, Vigman made available to Lugo proceeds generated from the sales of Nettie Vigman's inflated Aero Systems stock to finance FSSC's continued operation, and to increase FSSC's inventory of the target securities. The credit balance in Nettie Vigman's account effectively provided Lugo with an interest free loan of more than $220,000 in April 1981 (Foley Decl. ¶¶ 27, 34).

By the end of April 1981 Lugo was aware of FSSC's capital deficiency problem. He then ceased withdrawing his monthly compensation from the firm. Lugo used his salary and trading profits to relieve FSSC's deteriorating financial condition. At the close of the April reporting period for net capital, Lugo had to pay Nettie Vigman her

credit balance. In order to do this, Lugo borrowed $100,000 from SCCP, and to conceal FSSC's financial condition, the loan was not recorded in FSSC's Customer Loan Account (Foley Decl. ¶¶ 27, 39-42).

By May 29, 1981, FSSC had a net capital deficiency of $102,165. FSSC's inventory, adjusted to correct for securities parked by Holmes and others totaling ($213,125) was $619,000. The deficiency in FSSC's Customer Reserve Account was now $420,917. Again, to pay Nettie Vigman, Lugo borrowed $300,000 from SCCP, which was not reported in FSSC's Customer Loan Account (Foley Decl. ¶¶ 35, 39, 47).

As a result of the "parks" in the accounts of Holmes and others, Lugo was able to create the appearance of capital compliance and FSSC's financial deterioration was shielded from the NASD. (Foley Decl. ¶ 36-38, 43)

Had FSSC ceased doing business in May 1981, FSSC's calculated losses would have been $779,594. However, by FSSC continuing in business through July 24, 1981, FSSC's losses increased to $2,634,976 (Foley Decl. ¶¶ 83-86).

Without Holmes' participation in the May 1981 parking transaction, FSSC could not have created the appearance of net capital compliance. The concealment of FSSC's true financial condition allowed Lugo to continue in business, and as a result, the financial condition of FSSC worsened. FSSC's continued operation after May 29, 1981, permitted the following to take place:

a. FSSC continued to build up its inventory in Bunnington and Aerosonic stock;

b. FSSC's Customer Loan Account increased by $1,000,000 at SCCP;

c. FSSC's net capital deficiency and related losses increased by more than $1.8 million; and

d. FSSC's trading losses and reserve deficiency increased from $779,594 (as of May 29, 1981) to $2,634,976 (as of July 24, 1981) (Foley Decl. ¶¶ 81, 86).

2. SEBAG. – May 29 to July 27, 1981

On May 29, 1981, Sebag had total capital of $1,900,000. There was only $110,000 of Aerosonic, Bunnington, Dash and Osrow Stock in inventory (Foley Decl. ¶ 64). However, during June and July 1981, Garrity purchased more than $7,000,000 worth of these stocks from FSSC and other market makers to stabilize the market price of the securities. Of this amount, 95% of the securities purchased were in Bunnington, Aerosonic and Osrow. These securities were sold to the accounts of Garrity, his family members, and other customers. However, 46% of these purchases were ultimately never paid for and were purchased into Sebag's inventory pursuant to Regulation T at a cost of $3,300,000 (Foley Decl. ¶¶ 65, 66, 67).

Of the purchases paid for, a substantial number were financed through margin accounts. These margin purchases increased Sebag's bank loans, for which Aerosonic, Bunnington and Aero Systems stock were pledged as collateral. Losses resulting from a decline in the value of pledged securities exceeded $5,000,000 when the price of Aerosonic dropped to $5.00 and Bunnington dropped from $12.00 to $2.50 by July 27, 1981 (Foley Decl. ¶ 70 72)

Had FSSC ceased operations at the end of May 1981 instead of July 24, 1981, the damages to both FSSC and Sebag would have been substantially less (Foley decl. ¶ 83-86). If FSSC had ceased trading in May 1981, Sebag would not have collapsed (Foley Decl. ¶¶ 64-69).

3. SIPC's liquidation of FSSC and Sebag

Pursuant to SIPA, liquidation proceedings were initiated against FSSC and Sebag on July 24 and July 27, 1981, respectively. Under the provisions of SIPA, SIPC paid a total of $12,453,475.26 to the Trustee of FSSC and Sebag.

The acts of Holmes as set forth above led to and were a substantial contributing factor to the losses and damages incurred by SIPC and the two trustees.

III

CONCLUSION

Holmes' activities as described in this memorandum are intentional and criminal, and were committed by Holmes not only for his own enrichment but to aid and abet the enrichment of Vigman, Diamond, Lugo, Garrity, Blumenthal and others.

Each historical relationship, each act and each profiting illustrates that Homes' conduct must, at the very least, be weighed by a jury. Homes did not act alone, and he didn't profit alone, as counsel for Holmes would have this Court believe. Holmes and the others, acting in concert since as early as 1966 must now sit in concert before a

jury so that their acts can be judged. Homes motion must be denied.

Dated:
September 20, 1988

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PROOF OF SERVICE

I, the undersigned, declare that I am, and was at the time of service of the papers herein referred to, over the age of 18 years and not a party to the action. I am employed in the County of Los Angeles, State of California, in which county the within-mentioned mailing

occurred. My business address is Sheppard, Mullin, Richter & Hampton, 333 South Hope Street, 48th Floor, Los Angeles, California 90071. I am familiar with the regular mail collection and processing practices of Sheppard, Mullin, Richter & Hampton for correspondence deposited for mailing with the United States Postal Service. I served the following document(s):

STATEMENT OF BACKGROUND AND FACTS

by placing a copy in a separate envelope for each addressee named hereafter, addressed to each such addressee respectively as follows:

Please see attached Service List

I then sealed the envelope with postage thereon fully prepaid and deposited it for collection and mailing via the United States Postal Service on September 21, 1988. The envelope was sealed and deposited in accordance with the ordinary business practices of Sheppard, Mullin, Richter & Hampton for mailing on September 21, 1988

I declare under penalty of perjury under the laws of the State of California and the United States of America that I am employed in the office of a member of the bar of this Court at whose direction the service was made and that the foregoing is true and correct.

Executed on September 21, 1988, at Los Angeles, California.

/s/ Laura Lawrence

Z0531030.E1

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